87-846

Supreme Court, U.S.
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No. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A.T. DAVIS, A.T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A.T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T.C. DAVIS, II, T. C. DAVIS, II TRUST, T.C. DAVIS, II TRUST "A", T.C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T.C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.

Respondents

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTIONS PRESENTED

On November 24, 1986, a United States bankruptcy judge entered an order confirming a plan of reorganization under chapter 11 of title 11 of the United States Code for two corporate debtors. While appeals were pending in the United States District Court, the bankruptcy judge revealed that throughout the bankruptcy proceedings he owned stock in J.P. Morgan Co., Inc., holding company of Morgan Guaranty Trust Co. Morgan Guaranty was a major creditor, a signatory to the involuntary bankruptcy petition, a member of the creditors' committees of both debtors, and a proponent of the confirmed plan. Petitioners' motion to vacate the order confirming the plan of reorganization and related orders was denied by the District Court and this decision was affirmed by the United States Court of Appeals for the Fifth Circuit.

The questions presented are:

1. Is a bankruptcy judge disqualified under 28 U.S.C. § 455(b) if, based on the objective facts, he should have known that he owned stock in a corporate party? Is ownership of stock in the holding company-parent the ownership of stock in a bank-subsidiary for purposes of 28 U.S.C. § 455(b)(4)?

2. Where a bankruptcy judge has forgotten, neglected or overlooked that he owns stock in a party, are orders entered by said judge invalid if the issue is timely raised? If so, is the issue timely raised if it is raised during the appeal process?

3. When it is revealed post-judgment that a bankruptcy judge held stock in a corporate party to the proceedings before him, should a hearing be held to determine whether the judge knew or should have known that he held such stock at the time of the entry of the orders in question?

PARTIES TO PROCEEDING BELOW

In addition to the parties named in the caption of this case, the following were made parties to the proceeding in the Fifth Circuit:

The Bank of New York
The Chase Manhattan Bank, N.A.
Credit Commercial De France, New York Branch
Cummins Sales & Service, Inc.
Den Norske Creditbank
Development Bank of Singapore Limited
First City National Bank of Fort Worth
First City National Bank of Houston
First Interstate Bank of California
First National Bank & Trust Company of Oklahoma City
First National Bank of Fort Worth
First RepublicBank Dallas, N.A.
First RepublicBank Fort Worth, N.A.
Frigette Corporation
Geodril, Inc.
Globe Machinery and Supply Company
Harrisburg, Inc.
Interfirst Bank Fort Worth, N.A.
Irving Trust Company
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers Eastern Hemisphere, Inc.
Loffland Brothers (Singapore) Pte., Ltd.
Mechanical Rubber Products Corporation
Miami-Dickerson Steel Company
Midco Equipment Co.
Mid-Continent Supply Co.
Moore & Sons, Inc.
Morgan Guaranty Trust Company of New York

The National Commercial Bank of Saudi Arabia
Nippon Kokan Kabushiki Kaisha
Rig-A-Lite Company, Inc.
Security Pacific National Bank
Sligo, Inc.
State Pipe & Supply Co.
Texas American Bank (Fort Worth), N.A.
Unit Rig & Equipment Co.

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No. _____

K.W. DAVIS, JR., et al.,

Petitioners

v.

OFFICIAL UNSECURED CREDITORS' COMMITTEES et al.,

Respondents

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Petitioners[1] ("Petitioners") respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

OPINIONS BELOW

The *per curiam* opinion of the United States Court of Appeals for the Fifth Circuit is unreported and is reprinted in the appendix to this petition at Appendix p. 6 ("App.-6" hereafter). The Memorandum Order of the United States District Court for the Northern District of Texas, Dallas Division, is unpublished and is reprinted at App.-11.

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[1] The notices of appeal were filed by all Petitioners plus T.C. Davis. T.C. Davis was replaced as an appellant by his bankruptcy trustee, Twalla Dupriest, by order of the Fifth Circuit entered September 16, 1987.

JURISDICTION

The judgment of the court of appeals was entered on September 24, 1987. No petition for rehearing was filed. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1982).

STATUTE INVOLVED

The statutory provision involved in this case, 28 U.S.C. § 455 (1982), is set forth at App.-3.

STATEMENT

On February 21, 1985, certain bank creditors filed involuntary petitions for relief under chapter 11 of title 11, United States Code ("Code" or "Bankruptcy Code" hereafter) against Kendavis Holding Company ("KHC") and Kendavis Industries International, Inc. ("KIII")[2] (collectively "Debtors"). On March 11 and 13, 1985, respectively, orders for relief were entered as to KHC and KIII. On November 24, 1986, certain orders and findings were entered by United States Bankruptcy Judge Robert C. McGuire (the "Bankruptcy Court Orders") that confirmed a plan of reorganization for KHC and KIII (the "Plan") which was proposed by the Official Unsecured Creditors' Committees for each Debtor (the "Creditors' Committees").[3] The Committees'

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[2] KIII is a wholly-owned subsidiary of KHC. Petitioners are all the former equity owners of KHC. Additionally, K.W. Davis, Jr., Kay Davis and T.C. Davis were each holders of Class 6 claims under the plan of reorganization.

[3] The members of the KHC Creditors' Committee are Security Pacific National Bank, The Bank of Nova Scotia, Morgan Guaranty Trust Company of New York, Continental Illinois National Bank and Trust Company of Chicago, The Bank of New York,

Plan was confirmed by "cram down" pursuant to Bankruptcy Code § 1129(b)(1). Petitioners are bound by the provisions of the Plan under Bankruptcy Code § 1141. Under the Plan, Petitioners' equity securities are cancelled. Notices of appeal of the Bankruptcy Court Orders were timely filed by Petitioners on December 4, 1986.

By telephone conference hearing on March 23, 1987, Judge McGuire informed counsel for the Debtors and the Creditors' Committees that, individually and as a trustee of two trusts, he owned stock in J.P. Morgan Company, Inc. ("J.P. Morgan") and had done so throughout the period of these bankruptcy cases.[4] See App.-18 for transcript of telephone conference and App.-22 for March 20, 1987 issue of *The Value Line Investment Survey ("Value Line")* (an investment report regularly received by the judge).[5] Morgan Guaranty Trust Company of New York ("Morgan Guaranty") is a major creditor, a signatory to the involuntary petitions against the Debtors, and a member of the Committees. The holding company for Morgan Guaranty is J.P. Morgan. App.-25. Substantially all of the assets and business of J.P. Morgan are

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MBank Houston, N.A., First Interstate Bank of California, Irving Trust Company, Chase Manhattan Bank, N.A., Interfirst Bank Dallas, N.A., First City National Bank of Houston, and Credit Commercial de France, New York Branch. Membership of the KIII Creditors' Committee is identical with the membership of the KHC Creditors' Committee, except that the First National Bank & Trust Company of Oklahoma City is a member of the KIII Committee only. They will be referred to herein collectively as "Creditors' Committees".

[4] On Mar. 26, 1987, this stock had a market value of $36,057. Wall St. J., Mar. 27, 1987.

[5] Each of these documents was attached to Petitioners' Motion to Vacate filed in the district court and are part of the appellate record.

derived from Morgan Guaranty. *Id.* Judge McGuire recused himself on March 26, 1987.

On March 26, 1987, United States District Judge A. Joe Fish entered various orders and judgments (the "March 26 Orders") affirming the Bankruptcy Court Orders.

On March 31, 1987, the Petitioners filed in the district court a motion to vacate the Bankruptcy Court Orders based on the bankruptcy judge's disqualification pursuant to 28 U.S.C. § 455.[6] The district court's jurisdiction was based on 28 U.S.C. § 1334 and § 158 (1982 & Supp. II 1984). This motion was denied on April 10, 1987, by the district court's Memorandum Order. App.-11.

On April 13, 1987, the Petitioners filed a notice of appeal and a motion for an expedited appeal.[7] The expedited appeal was granted by the Fifth Circuit by order of April 15, 1987.[8]

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[6] This section is expressly applicable to bankruptcy judges pursuant to Bankruptcy Rule 5004(a).

[7] Prior to the entry of the Memorandum Order denying the motion to vacate, a notice of appeal of the March 26 Orders and motion for an expedited appeal had been filed. The second notice of appeal and motion for expedited appeal included all issues previously raised and added the Memorandum Order and the district court's Order Granting Committees' Motion to Quash Notice of the Davises to Take Deposition of the Honorable Robert C. McGuire, United States Bankruptcy Judge ("Order Quashing Deposition"). App.-31

[8] The appeal was originally orally argued before the Fifth Circuit on June 3, 1987. Subsequently, parties were informed that all three circuit judges hearing oral argument had disqualified and the case was to be reargued September 16, 1987. The second panel was composed of two senior circuit judges because of the disqualification or unavailability of other active circuit judges. App.-9 and 8.

REASONS FOR GRANTING THE WRIT

At the time he entered orders which, among other things, cancelled the equity securities owned by Petitioners, the bankruptcy judge owned $36,000 worth of publicly traded stock in J.P. Morgan. The plan confirmed was supported and proposed by Morgan Guaranty — wholly-owned subsidiary of J.P. Morgan. The bankruptcy judge did not disqualify as required by 28 U.S.C. § 455(b)(4) because he failed to recognize that substantially the entire business of J.P. Morgan was the ownership of Morgan Guaranty. He did not realize this, in spite of the fact that he recognized the similarity of names early in the proceedings and that he regularly received *Value Line* which clearly revealed the J.P. Morgan/Morgan Guaranty relationship. The public's perception of the impartiality of the bankruptcy judge can, by its very nature, only focus on the fact of ownership and the judge's possession of information revealing the relationship. From this information it can reasonably be concluded that the judge should have known that he owned a financial interest in Morgan Guaranty. Since he objectively should have known, he must be concluded to have known in light of his statutory duty to inform himself of his own financial interest under § 455(c). A party cannot escape the consequences of a statutory duty to be informed by the *ipse dixit* that he failed to notice. If true of the public at large, it must certainly be true of the federal judiciary which holds the public to such standards. It simply will not do for the judiciary to be perceived as applying one standard to itself and the brethren of the bench and another standard to litigants that come before that bench. Tolerance of judicial decisions rendered by judges owning financial interests in a party, however small, are not dangerous merely or principally because they are likely to in fact subjectively bias the decision. The greater danger is that, being perceived by the public as questionable practices, they will undermine the

public's confidence in the impartiality of that judiciary — an impartiality without which the judiciary will fail of its essential function.

Nevertheless, the district court accepted Judge McGuire's unsworn *ipse dixit* as to the facts concerning his knowledge of his financial interest, denied Petitioners their request to depose Judge McGuire (relief opposed by Respondent Committees and not by Judge McGuire), and held that § 455(b)(4) requires "actual prior knowledge" (App.-14) and that "a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual or constructive knowledge of any conflict." App.-15-16. The Fifth Circuit affirmed stating "the district judge was entitled to accept the bankruptcy judge's statement of his lack of knowledge that the corporation in which he held stock was the corporate parent of a creditor of the bankrupt debtor and might be affected by the outcome of the proceeding." App.-7.

Review of this decision is merited, therefore, because it presents important questions never heretofore treated by this Court concerning the duties of a judge to be informed about his own financial interests in a corporate party and the effect of those interests on his duty to disqualify under 28 U.S.C. § 455 (1982). These issues vitally affect the federal judiciary and especially affect the bankruptcy courts and their administration of complex reorganization cases. The Fifth Circuit decision seriously departs from established law mandating a due process hearing of factual issues related to judicial disqualification.[9] The instant decision also departs from the

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[9] *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986) *cert. granted*, 107 S.Ct. 1368 (1987) (scheduled to be orally argued December 9, 1987); *Potashnick v. Port City Const. Co.*, 609 F.2d 1101 (5th Cir. 1980), *cert. denied*, 449 U.S. 820; and *Kinnear-Weed Corp. v. Humble Oil & Refining Co.*, 403 F.2d 437

Fifth Circuit decision in *Health Services Acquisition Corp.*, 796 F.2d 796 (5th Cir. 1986) *cert. granted*, 107 S.Ct. 1368 (1987)[10] on the applicability of a constructive knowledge test to 28 U.S.C. § 455(a).[11] Conflict exists among the circuits on the effect of rulings rendered by a judge who failed to disqualify as required by 28 U.S.C. § 455 and the requisite timing for raising disqualification issues which have been overlooked by the judge. Finally, this Court has never addressed the question of the purpose and effect of 28 U.S.C. § 455(b) as it relates to financial interests of a judge in a party or the corporate subsidiary of a party. All of these issues raise serious questions about the appearance of impartiality of the federal judiciary and thus impact the administration of justice in these courts.

1. The Bankruptcy Judge Was Disqualified at the Time the Bankruptcy Court Orders Were Entered Because He Owned Common Stock in the Bank Holding Company of a Major Bank Creditor.

The bankruptcy judge at all pertinent times had a "financial interest" in the corporate parent of a party to a proceeding before him. 28 U.S.C. § 455(b)(4) and § 455(d)(4). The pertinent issue under 28 U.S.C. § 455(b)(4) is whether the bankruptcy judge "knew" his interest in the holding company was an interest in the bank subsidiary. In any event, the

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(5th Cir. 1968), *cert. denied*, 404 U.S. 941 (1971). The decision below was participated in by two senior circuit judges because of the disqualification or unavailability of active circuit judges. See Certificate of Need filed by Chief Judge Clark on September 30, 1987. App.-8.

[10] Petitioners herein have filed an *amicus* brief in this Court in *Liljeberg v. Health Services Acquisition Corp.* (No. 86-957).

[11] This particular departure is not correctable by a rehearing *en banc* in light of the unavailability of Fifth Circuit judges. App.-8.

ownership of stock in a bank holding company of a major bank creditor creates a basis for reasonably questioning the judge's impartiality under 28 U.S.C. § 455(a).

(a) The Bankruptcy Judge Knew He had a Financial Interest Pursuant to 28 U.S.C. § 455(b)(4).

(1) *Historical Background.* In 1969 the U.S. Senate refused to confirm the nomination of circuit judge Clement Haynsworth to be an associate justice, in part, because of disclosures that on several occasions he had participated in decisions in which he held stock in a party, including three instances where he held stock in a corporate parent of a party, or in a corporation which was a substantial creditor of a party.[12] From the Senate debate came an agreement between Senator Birch Bayh and Senator Ernest Hollings to clarify then-existing legislation concerning judicial disqualification. *Senate Hearings*, p. 25 (testimony of Senator Hollings).

(2) *Section 455(b)(4) Focuses on the Appearance of Impropriety.* Senate Bill 1064[13] was partly the result of the Bayh-Hollings agreement and was enacted to bring the federal statutory requirements closer to the new ethical rules of the Code of Judicial Conduct of the American Bar Association

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[12] See *Note, Disqualification of Judges and Justices in the Federal Courts*, 86 Harv. L. Rev. 736 (1973) ("*Harvard Note*" hereafter) and *Judicial Disqualification: Hearing on S.1064 Before the Subcommittee on Improvements in Judicial Machinery of the Senate Committee on the Judiciary*, 93d Cong. 1st Sess. 1 (1973) ("*Senate Hearings*" hereafter) (opening statement of subcommittee chairman Quentin N. Burdick). (Hearings held on July 14, 1971, and May 17, 1973, were reported in a single document with consecutive pagination. The hearings of May 17, 1973, begin on page 73.)

[13] The Senate Bill 1064 amended 28 U.S.C. § 455 in 1974.

("A.B.A. Code"). It is based upon Canon 3C.[14] In amending 28 U.S.C. § 455 Congress was, of course, concerned with influences that actually and improperly affect the impartial administration of justice. But the ethical concerns noted in connection with the Haynsworth confirmation did not involve *any* evidence or accusation of actual bias by the judge because of his financial interests.[15] The *appearance* to others of possible partiality was the focus of these criticisms. Throughout the legislative history, the theme is the promotion and protection of public and litigant confidence in the impartiality of judicial decisions. Thus, while the appearance of impartiality is the general theme of § 455(a), it is also the pointed theme of § 455(b)(4).

Canon 3C(1) of the A.B.A. Code provides that "a judge should disqualify himself" where "his impartiality might reasonably be questioned. *including* but not limited to instances

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[14] *Senate Hearings*, p. 2; *S. Rep.* No. 93-419, 93d Cong. 1st Sess. 1 (1973) ("*Senate Report*" hereafter); H.R. No. 93-1453, 93d Cong. 2d Sess. 1 (1974) reprinted in 1974 *U.S. Code Cong. & Admin. News* 6,351 ("*House Report*" hereafter); and *Senate Hearings*, p. 113-14 (statement of John P. Frank). John P. Frank is perhaps the most prolific expert on judicial disqualification in the United States. Because of his landmark article on judicial disqualification cited below, he testified as an expert witness at the request of Senator James Eastland in connection with the Haynsworth confirmation hearings. Additionally, he testified twice before the Senate subcommittee and once before the House subcommittee on amending 28 U.S.C. § 455. He also worked with Senator Bayh on his initial bill. See *Senate Hearings*, p. 32, 13 and *Judicial Disqualification: Hearings on S.1064 Before the Subcommittee on Courts, Civil Liberties, and the Administration of Justice of the Committee on the Judiciary*, 93d Cong., 2d Sess. p. 8 (1974) ("*House Hearings*" hereafter) (testimony of John P. Frank).

[15] See *Sen. Exec. Rep.* No. 91-12, 91st Cong. 1st Sess. (1969) (individual views beginning at p. 40).

where: . . . (c) he knows that he . . . has a financial interest . . . in a party to the proceeding . . . ." (emphasis added). Thus, under the A.B.A. Code, having a financial interest was merely a specific instance where a judge's impartiality might be questioned.[16]

While the language in § 455 does not include the connecting phrase "including but not limited to" between subparagraph (a) and (b) as is found in Canon 3C(1), there is no reason to think that this difference is meaningful. Congress intended in § 455(a) to set up an objective and general standard to govern judicial disqualifications.[17] Thus lack of impartiality was not to be judged subjectively but where "there is a reasonable factual basis for doubting the judge's impartiality, he should disqualify. . . ." Section 455(b) listed specific situations in which a judge was disqualified to aid the judge "in avoiding possible criticism for failure to disqualify. . . ." [18]

The congressional theme reflects historical concerns that judicial decisions in a democracy derive their principal sanc-

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[16] See E. Thode, *Reporters Notes To Code of Judicial Conduct* p. 60 (1973) ("A.B.A. Reporter's Notes").

[17] *House Report* p. 5-6, see identical language in *Senate Report* p. 5. Similarly, see *Senate Hearings*, p. 80 (testimony of Judge Roger Traynor, Chairman of the A.B.A. Special Committee on Standards of Judicial Conduct and former Chief Justice of the California Supreme Court); p. 93 and 99 (testimony of Professor E. Wayne Thode, Reporter for the A.B.A. Special Committee on Standards of Judicial Conduct); and *Senate Hearings*, p. 30 (testimony of Senator Hollings).

[18] *House Report, id.*

tion from public confidence in their impartiality. Possessing "neither the purse nor the sword"[19] authority of courts

> rest[s] ultimately on public acceptability of judicial decision making. That acceptability depends in turn on a belief in the impersonality and reasoned foundation of judicial decisions. Such a belief is, of course, undermined when judicial decisions may be closely identified with the interests or prejudices of the decision makers themselves. (footnotes omitted)

Harvard Note p. 746-47.

The relation of a judge's ownership of a financial interest in a party, and the "appearance of impropriety," is evident from the congressional decision to make the size of the financial interest irrelevant. Congress was dissatisfied with the substantial interest standard of § 455 as it stood. Disqualification for holding a substantial interest addresses, albeit imprecisely, actual partiality in a judge. Disqualification for holding a small interest can only address appearances. Admittedly, judicial ownership of a financial interest in a party would not necessarily *in fact* influence a judge to an improper decision. However, to a fair, impartial observer, such ownership doubtless appears questionable.

Concerns also existed that the constitutional guarantee of due process of law was impugned where a judge had any interest.[20] (See pgs. 27-30, *infra*). Congress' solution was to require disqualification for any financial interest,[21] as had

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[19] *Baker v. Carr*, 369 U.S. 186, 267 (1962) (Frankfurter, J., dissenting).

[20] *Senate Hearings, p. 102* (testimony of Professor E. Wayne Thode).

[21] *House Report*, p. 2 and *Senate Report*, p. 2.

been the almost universal rule prior to 1948.[22] Disqualification for a small interest was seen as justified because it was impossible to know objectively the threshold of actual influence for all judges and no threshold avoids the appearance of impartiality absolutely.[23] As Judge Traynor said:

> An independent and honorable judiciary is an indispensable condition of justice in our society. It is not enough that people have confidence in the sturdiness of judicial procedure. They must have utmost confidence in the integrity of their judges. The basic purpose of the Code of Judicial Conduct is to assure that judges will be worthy of that independence and deserving of that confidence.

Senate Hearings, p. 80.

(3) *Knowledge of Financial Interest.* Under 28 U.S.C. § 455(b)(4), a judge is disqualified if he "*knows* that he . . . has a financial interest in . . . a party . . . " (emphasis added). Significantly, under § 455(c), a judge is required to "*inform himself* about his personal and fiduciary financial interest . . . " (emphasis added). Here, Judge McGuire admits that he possessed all of the objective facts showing that J.P. Morgan is the parent of Morgan Guaranty and that he regularly received the *Value Line* from which he actually, eventually discovered the relationship. App.-22.

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[22] *Senate Hearings*, p. 34 (testimony of John P. Frank) and Frank, *Disqualification of Judges*, 56 Yale L.J. 605, 627 (1947) ("*Frank Disqualification*" hereafter).

[23] See *Senate Hearings*, p. 15 and 16 (testimony of Senator Bayh); p. 26 (testimony of Senator Hollings); p. 46 (testimony of John P. Frank); and *House Hearings*, p. 9 (testimony of John P. Frank).

Congress deliberately distinguished between the judge's duty as to his own financial interests (for which he "has a duty to inform himself") and those of his spouse or minor children (for which he "must merely make a reasonable effort to inform himself").[24]

Wright, Miller and Cooper have noted that:

> The judge . . . is disqualified only if "he knows" of the financial interest. *Meaning is put into this*, however, by another provision of the amended statute that provides that a judge should inform himself about his personal and fiduciary financial interest, and make a reasonable effort to inform himself about the personal financial interest of his spouse and minor children residing in his household. (emphasis added)

13A Wright, Miller and Cooper, *Federal Practice and Procedure* § 3546, p. 600 (1984). The *Harvard Note*, footnote 66 p. 752, states that "as a corollary to the [A.B.A.] *Code's* provisions requiring disqualification on account of financial interests, Canon 3C(2) requires a judge to 'inform himself about his personal and fiduciary financial interests.' "

Congress did not intend to permit a judge to escape the provisions of § 455(b)(4) by oversight. The district court and the Fifth Circuit in the instant case mistakenly turn § 455(c) into a requirement that in all cases the judge need only make reasonable inquiry for the judge's statement alone negates any responsibility for his failure to adhere to § 455(c). This interpretation negates the distinctions clearly set out in § 455(c).

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[24] *House Report*, p. 6-7, and *Senate Report* p. 6.

Congress was clearly aware of the significance of this obligation. In the House Hearings the following exchange took place between Congressman Cohen and Judge Traynor:

> "Mr. Cohen. . . . as I understand it, this would prohibit any kind of financial interest of a judge sitting on a case in which he might have any kind of an interest, is that correct?
>
> Judge Traynor. That is right.
>
> Mr. Cohen. That would take in a situation I assume that if a fairly wealthy judge has several million dollars in assets, let's say tied up in perhaps a blind trust or some sort of a portfolio, would he be required, under this legislation, to review each and every stock that he had?
>
> Judge Traynor. Yes, he is obliged to, and in a way repudiate the blind trust device.
>
> Mr. Cohen. So he has a continuing obligation constantly to review whatever assets he might have in the form of stocks?
>
> Judge Traynor. That is right, and there is an exception here for mutual funds, because of the impossibility of keeping track of a portfolio of a mutual fund.

House Hearings, p. 15-16.

John P. Frank informed Congress as regards § 455(c):

> This provision requires the judge to be informed about his own personal financial interests and calls upon him to make a reasonable effort to know about those of the relations who might, by virtue of their holdings, cause him to be disqualified. There are highly practical problems here. Some people hold a wide number of stocks, or maintain portfolios in which there may be

> considerable turnover. There exists the possibility of disqualification in fact where the judge does not know that he has a particular investment. I read this provision to be virtually a requirement that those judges who have extremely disbursed holdings must make an effort to consolidate them; *they will not be excused for failing to know what they have*. On the other hand, they clearly cannot as well know of varying investments of relatives, and here all that is required is "a reasonable effort." (emphasis added)

Senate Hearings, p. 115 (statement of John P. Frank).

Thus, the combination of § 455(b)(4) and the duty to be informed as to personal and fiduciary investments under § 455(c) establish a standard by which a judge is charged, conclusively, with knowledge of that which information in his possession reveals about his financial interest or which reasonable inquiry would reveal.

Any other position vitiates § 455(b)(4). Not only do such judicial interests create public and litigant doubt about the fairness of decisions, but such interests themselves undermine the fairness of the process whether or not they consciously affect the judge's decision. As Justice Frankfurter said in recusing himself on the ground of personal bias in *Public Utils. Comm'n v. Pollak*, 343 U.S. 451, 466 (1952):

> The fact is that, on the whole, judges do lay aside private views in discharging their judicial functions. This is achieved through training, professional habits, self-discipline and that fortunate alchemy by which men are loyal to the obligation with which they are entrusted. But it is also true that reason cannot control the subconscious influence of feelings of which it is unaware. When there is ground for believing that such unconscious feelings

> may operate in the ultimate judgment, or may not unfairly lead others to believe they are operating, judges recuse themselves. They do not sit in judgment. They do this for a variety of reasons. The guiding consideration is that the administration of justice should reasonably appear to be disinterested as well as be so in fact.

No reason appears in the text, history, or policy of § 455 for distinguishing between (1) the constructive knowledge derived from the possession of revealing information and the duty to be informed, and (2) knowledge of a financial interest under § 455(b)(4). Neither forgetfulness, oversight, nor neglect are "the sort of objectively ascertainable fact[s] that can avoid the appearance of partiality." *Health Services Acquisition Corporation v. Liljeberg*, 796 F.2d 796, 802 (5th Cir. 1986) *cert. granted*, 107 S.Ct. 1368 (1987).[25]

"Whenever inquiry is a duty, the party bound to make it is affected with knowledge of all which he would have discovered had he performed the duty. Means of knowledge with the duty of using them are, in equity, equivalent to knowledge itself." *Cordova v. Hood*, 17 Wall. (84 U.S.) 1, 8 (1873). In *King v. United States*, 379 U.S. 329 (1964), a corporate officer was held liable as distributing agent to the government on a priority claim in bankruptcy for having paid non-priority creditors. He was bound by his duty to know the status of assets and claims and his subjective, conscious awareness was

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[25] The court in *Health Services* distinguished § 455(a) and § 455(b)(4) based upon the statutory use of the word "know" in § 455(b)(4) which was absent in § 455(a). The court did not discuss whether this distinction was of significance and the reasoning of the court as to the § 455(a) problem is directly applicable to the § 455(b)(4) problem — at least in the context where the information is unambiguously available in the judge's own records. See *infra*.

irrelevant. See 379 U.S. at 339-40. In the instant case the judge had an explicit duty to stay informed. This duty corresponded fully with the congressional expectations. How can the public and losing litigants be satisfied by being told the judge failed to know what he owned?

Public perceptions will, and must, focus on the objective facts. The subjective "conscious awareness" relied on below[26] is ever shielded from public view. An assessment of a judge's knowledge of his own financial interests by an objective appraisal of the facts is the only means of supporting the congressional purpose in 28 U.S.C. § 455. The public's confidence of neccesity will be measured by the public's perception of events. This must be measured, not by rumor and innuendo, but by an appraisal of the objective facts. Thus, whether a judge knew of a financial interest for purposes of § 455(b)(4) must be determined from the information available to the judge, in light of the judge's duty to be informed about that financial interest and consequent duty to disqualify. Under the facts in this case on the limited record,[27] Petitioners believe that the judge was disqualified at the time of the entry of the challenged orders.

In this case, on an objective basis, Judge McGuire must be said to have known that he owned stock in J.P. Morgan and that it was significantly related to Morgan Guaranty. He held this stock personally and as a fiduciary. Virtually the sole business activity of J.P. Morgan is the ownership of Morgan Guaranty. Ownership of Morgan Guaranty is the only possible reason one would own stock in J.P. Morgan. He was regularly furnished the *Value Line* which on its face and

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[26] And followed by the court in *NEC Corp. v. Intel Corp.*, 654 F. Supp. 1256 (N.D. Cal. 1987).

[27] See *infra pgs.* 27-29.

unambiguously revealed the ownership of Morgan Guaranty by J.P. Morgan. Moreover, he had a duty under § 455(c) to inform himself as to his personal and fiduciary financial interests as well as a state law based duty as a fiduciary to be aware of said holdings. The judge's actual, subjective integrity is not called into question. But an objective test is essential to protect the public and litigant confidence in the judge's impartiality.

(b) The Bankruptcy Judge's Interest In the Holding Company-Parent of a Party is the Ownership of a Financial Interest In a Party Under 28 U.S.C. § 455(b)(4).

The Fifth Circuit has noted that "[t]he Advisory Committee on Judicial Activities of the Judicial Conference of the United States concluded that a judge should disqualify himself when a controlled subsidiary of a corporation in which he owns stock is a party." (Footnotes omitted) *Weingart v. Allen and O'Hara, Inc.*, 654 F.2d 1096, 1107 (5th Cir. 1981). *See also Catherines v. Copytele, Inc.*, 608 F. Supp. 1031 (E.D.N.Y. 1985) and *Harvard Note*, p. 753.

In this case, substantially all the assets and business of J.P. Morgan are derived from Morgan Guaranty such that a financial interest in J.P. Morgan is indistinguishable from a financial interest in Morgan Guaranty for purposes of 28 U.S.C. § 455. If ownership of stock in a corporate party litigant requires disqualification in order to ensure the appearance of impartiality, it is equally necessary to disqualify a judge for stock ownership in a bank holding company whose subsidiary bank makes up 95% of the holding company's assets — especially one of the stature of J.P. Morgan/Morgan Guaranty.

(c) The Ownership of Stock in the Bank Holding Company of a Major Creditor Establishes a Reasonable Basis for Questioning the Judge's Impartiality.

The Petitioners argue above that disqualification under 28 U.S.C. § 455(b)(4) is merely a specific and more precise instance of disqualification where the judge's "impartiality might reasonably be questioned" as provided in 28 U.S.C. § 455(a). The argument is based upon the history behind the 1974 amendments to § 455. Nevertheless, the Fifth Circuit has drawn a distinction between § 455(b)(4) and § 455(a) by noting that "§ 455(a) does not explicitly require knowledge." *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d at 802. Petitioners argue herein that the knowledge requirement of § 455(b)(4), when applied to a judge's own financial interest, cannot be evaded by subjective factors such as memory or failure to recognize what the objective facts clearly state. This argument comes close to, if it is not identical with, the "constructive knowledge" view of § 455(a) taken in *Health Services*. Petitioners also assert that the bankruptcy judge had sufficient information in hand and a sufficient interest in a party that his impartiality might reasonably be questioned under § 455(a).

In *Health Services*, the court held that the trial judge had constructive knowledge of what he had known but had forgotten and observed that the "judge's forgetfulness, however, is not the sort of objectively ascertainable fact that can avoid the appearance of partiality." 796 F.2d at 802. So it is here. Judge McGuire was aware of his J.P. Morgan stock ownership and regularly received reports which on their face indicated that J.P. Morgan owns Morgan Guaranty. Morgan Guaranty is the predominant business of J.P. Morgan and the sole business discussed in the *Value Line* reports regularly received by the bankruptcy judge. He had a mandatory duty

to inform himself about his financial interests. These facts alone objectively establish that the bankruptcy judge had an interest in a party and constructively knew that he had an interest in that party. The judge's stated unawareness of the relationship between J.P. Morgan and Morgan Guaranty is "not the sort of objectively ascertainable fact that can avoid the appearance of partiality." *Id.*

2. The Challenged Orders Are Invalid.

(a) Only Vacation of The Judgment and a New Trial Adequately Protect the Public's Expectation of Impartiality.

Conflict exists among the circuits as to the appropriate judicial reaction where challenges are made post-judgment to orders entered by a judge disqualified under 28 U.S.C. § 455. The Fifth Circuit has concluded that a judgment entered by a judge in circumstances where the judge's impartiality might be questioned on an objective basis must be vacated. *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d at 802 and 803. The Seventh Circuit has concluded that disqualification under § 455(a) for mere appearance of partiality operates only prospectively from the time of the motion in the absence of actual bias. *United States v. Murphy*, 768 F.2d 1518, 1539 (7th Cir. 1985), *cert. denied*, 475 U.S. 1012 (1986). The Ninth Circuit has concluded that "if the judge had knowledge within the meaning of... [Section 455(b)(4)] at the time he sat, all his rulings must be vacated." *Davis v. Xerox*, 811 F.2d 1293, 1296 (9th Cir. 1987), *petition for cert. filed* (July 6, 1987).

As the Fifth Circuit has said: "[g]enerally, a judge who learns he has a financial or other interest in a case is only required to recuse himself from future proceedings." *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d at 801. This is,

of course, the way Congress hoped the statute would work. The duty to disqualify is that of the judge. If done optimally, disqualification will happen early and a new judge be assigned. But this cannot happen when a judge overlooks, ignores, or forgets a financial interest in a party.

Respondents below would simply say that it is harmless error if a judge fails in his duty to disqualify where information available to him reveals a disqualifying financial interest unless actual bias is shown. In all cases of judicial amnesia, they would say there is no remedy. But they fail to say how this furthers the congressional interest in encouraging public confidence in judicial impartiality.

Petitioners have argued above that 28 U.S.C. § 455(b) identifies grounds to disqualify a judge because these grounds suggest partiality to the public and not because they always or usually result in biased decisions. Contrary views, not based on a full review of the legislative history, are ennunciated by the Seventh Circuit in, e.g., *United States v. Murphy*, 768 F.2d at 1539-41. If Petitioners are correct, and holding interests as defined in § 455(b)(4) results in disqualification in part because failure to do so undermines public and litigant confidence in the impartiality of the judiciary, then failure to provide a post-judgment remedy inadequately secures the protected interest.

The statute contains no express remedy for this situation. The legislative history reflects opinions running from reversal so long as the matter pends on appeal to collateral attack.[28]

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[28] *Senate Hearings*, p. 22 (testimony of Senator Bayh: indicating that the issue should be resolved within the appeal process based on timely objection); *Senate Hearings*, p. 36 (testimony of John P. Frank: "It is my view that if the judge turns out at the appeal stage to have had any interest, it is reversable error."); *House Hearings*, p. 16-17 (testimony of Judge Traynor: "That is whether

Nowhere does any part of the legislative history suggest that there is no remedy where a judge has overlooked, ignored or forgotten a disqualifying interest and gone ahead and participated in a case.

The judicial function in cases like this must be to formulate and apply a remedy which will effectuate the goals set out in the statute. The principal goal of the 1974 amendments is to

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a judge who sits in violation of these standards, whether the judgment that he enters is then subject to collateral attack [sic]. It would be my judgment that where his disqualification was for financial interest, and he did not keep track of his interests or if he deliberately sat despite the financial interest, thinking that, say, five shares in General Motors was insubstantial, in violation of our more heroic provision that any interest, however small, would raise a serious question as to whether that judgment would be subject to collateral attack. [at 16] . . . I think there is strong support for the proposition that a judge who sits in violation of the financial interest disqualification would subject his judgment to collateral attack. [at 17]"); *House Hearings*, p. 16-17 (testimony of John P. Frank: " . . . should he have a misunderstanding or misinterpretation of the matter, he is subject to review. He is subject to mandamus and he is subject to reversal. [at 16] . . . I would say, if I might supplement, it is subject to direct attack without question. The question of collateral attack, whether it reaches the point that it becomes, as the Judge has said, a denial of due process and is so void or whether it is mere error would require a set of qualifications that is beyond the scope of this bill or our commentary. [at 17]"); and 120 Cong. Rec. 36,269 (1974) (statement of Rep. Kastenmeier: "It may be noted that neither existing nor proposed section 455 contains a sanction to enforce compliance. The section simply requires self-disqualification. The judge may be petitioned to disqualify himself. Failing this, he may be admonished. He may be reviewed, he may be mandamused and he may be reversed. The chief judge of the circuit may remove him from a particular case and, ultimately, a judge could be impeached and removed for failure to maintain 'good behavior'.")

assure the public and losing litigants that judicial decisions will be or have been made on the merits and not affected by taint of the interests of individual judges. This taint need not be the conscious pursuit of interest[29] but will often be an inclination borne of an interest which tips "the scales of justice."[30] To be adequate, the remedy must remove the grounds for public doubt about judicial impartiality. This doubt arises when reasonable people would infer "that a judge has knowledge of facts that would give him an interest in the litigation." *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d at 802.

(b) Entry of Orders by a Judge Holding a Financial Interest in a Party Deprives the Other Parties of Due Process of Law.

"No person shall . . . be deprived of . . . liberty, or property without due process of law." U.S. Const., Amend. V. In *Tumey v. Ohio*, 273 U.S. 510 (1927) the Court held that the petitioner was denied fourteenth amendment due process when he was tried by a judge who received as compensation a small portion of the fine when he convicted persons. In *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968) *reh'g denied*, 393 U.S. 1112 (1969), the Court held that an arbitration award should not be enforced where the impartial arbitrator failed to disclose that he owned an interest in a company that sporadically rendered services for a party to the arbitration which generated about $12,000 in fees to the arbitrator's company over a four to five year period.

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[29] See *Public Utils. Comm'n v. Pollak*, 343 U.S. 451, 466 (1952), quoted *supra* pgs. 15-16.

[30] Letter from Prof. David Mellinkoff to Sen. Griffin dated Oct. 20, 1969, as reported in Sen. Exec. Rep. No. 91-12, 91st Cong., 1st Sess. 46 (1969) (individual views of Sen. Griffin).

The court stated "[s]ince in the case of courts this is a *constitutional* principle, we can see no basis for refusing to find the same concept in the broad statutory language that governs arbitration proceedings . . ." 393 U.S. at 148 (emphasis original). "A fair trial in a fair tribunal is a basic requirement of due process. Fairness, of course, requires an absence of actual bias in the trial of cases. But our system of law has always endeavored to prevent even the probability of unfairness. To this end no man can be a judge in his own case and no man is permitted to try cases where he has an interest in the outcome." *In re Murchison*, 349 U.S. 133, 136 (1955).

The content of due process is derived in part from "those settled usages and modes of proceeding existing in the common and statute law of England . . ." *Tumey*, 273 U.S. at 523. "There was at the common law the greatest sensitiveness over the existence of any pecuniary interest however small or infinitesimal in the justices of the peace." *Tumey*, 273 U.S. at 525. Direct pecuniary interest is the oldest common law basis for judicial disqualification. *Frank Disqualification*, p. 609. In *Ward v. Village of Monroeville*, 409 U.S. 57 (1972), the Court expanded *Tumey* to invalidate judgments entered by a judicial officer who also had executive responsibilities in a city where the court produced a substantial portion of the city's funds, i.e., any supposed benefit to the judge arose indirectly. As the Court said in *Commonwealth Coatings*:

> Although in *Tumey* it appeared the amount of the judge's compensation actually depended on whether he decided for one side or the other, that is too small a distinction to allow this manifest violation of the strict morality and fairness Congress would have expected on the part of the arbitrator and the other party in this case. Nor should it be at all relevant . . . that "[t]he payments received were a very small part of [the arbitrator's]

> income . . . ." For in *Tumey* the court held that a decision should be set aside where there is "the slighest pecuniary interest" on the part of the judge and specifically rejected the state's contention that the compensation involved there was "so small that it is not to be regarded as likely to influence improperly a judicial officer in the discharge of his duty . . . ." ". . . in the case of courts this is a constitutional principle . . . ."

393 U.S. at 148.

In *Aetna Life Insurance Co. v. Lavoie*, 475 U.S. 813, 106 S.Ct. 1580 (1986), the Court vacated a judgment affirmed by the Alabama Supreme Court because one of the participating justices had initiated actions on legal theories similar to that in *Lavoie* during the period of the Alabama court's consideration of that case. This conflict was not discovered until a motion for rehearing was pending in the Alabama Supreme Court. This Court held that the affirmance of such a judgment violated fourteenth amendment due process, not because the judge was influenced by his interest, but because the interest might offer a temptation to the average judge to tip the nice balance of decision-making. *Lavoie*, 106 S.Ct. at 1587. "[T]o perform . . . [justice's] high function in the best way, 'justice must satisfy the appearance of justice.'" *Id*, citing *Murchison*, 349 U.S. at 136.

Like the Senate and House Committees[31] and like Judge Traynor[32] and Professor Thode,[33] Petitioners believe that these cases strongly suggest, if they do not hold, that a judicial decision rendered by a judge owning a financial

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[31] *House Report*, p. 7 and *Senate Report*, p. 6.

[32] *House Hearings*, p. 17.

[33] *Senate Hearings*, p. 95.

interest in a party at the time the decision is rendered denies a litigant of its due process right to an impartial hearing. Such a denial renders the judgments entered *void*.[34]

(c) Disqualification is Jurisdictional.

Numerous state courts have held that statutes and constitutional provisions disqualifying judges because of interests are jurisdictional and orders entered by disqualified judges are void.[35] No federal cases have been found considering the relation between disqualification of judges and jurisdiction.

Petitioners argue that 28 U.S.C. § 455 is jurisdictional. Section 455 is mandatory and establishes standards for disqualification of federal judges. The only constitutional basis for Congress to limit the authority of federal judges is its power to establish such courts, inferior to the Supreme Court, as it deems appropriate and to regulate the appellate jurisdiction of the Supreme Court. U.S. Const., Article III, Sections 1 and 2. Because of these powers, the jurisdictional authority of federal courts under article III of the United States Constitution is not considered self-executing, but may be limited by Congress. *Cary v. Curtis*, 3 How. (44 U.S.) 236 (1845); and *Palmore v. United States*, 411 U.S. 389 (1973).

If the authority to disqualify judges by statute is derived from Congress' authority to regulate the jurisdiction of federal courts, it follows that § 455 is jurisdictional and decisions

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[34] *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980).

[35] *See, e.g., Gaer v. Bank of Baker*, 107 P.2d 877 (Mont. 1940); *Buckholts Indep. School Dist. v. Glaser*, 632 S.W.2d 146 (Tex. 1982); *Casterella v. Casterella*, 409 N.Y.S.2d 548 (N.Y. App. Div. 1978); and, *generally*, Annotation, *Disqualification Of Judge Because Of His Or Another's Holding Or Owning Stock In Corporation Involved In Litigation*, 25 A.L.R.3d 1331 (1969).

made by disqualified judges are void as beyond the court's jurisdiction.[36] No reason is apparent for treating the matter of judicial incompetence to act because of a disqualification differently from that of subject matter jurisdiction. In both cases, the interest of the judiciary and public in the reality and appearance of judges' impartiality transcends the interests of the litigants. Cf. *Kinnear-Weed Corp. v. Humble Oil & Refining Co.*, 403 F.2d 437 (5th Cir. 1968), *cert. denied*, 404 U.S. 941 (1971); *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986), *cert. granted*, 107 S.Ct. 1368 (1987); and *Commodity Futures Credit Comm'n v. Schor*, __ U.S. ___, 106 S.Ct. 3245 (1986).

Since the jurisdiction of bankruptcy judges is derived from the jurisdiction of the district courts and is created by the discretionary reference of such matters to the bankruptcy judges by the federal district court, 28 U.S.C. §§ 1334 and 157 (1982 and Supp. II 1984), the disqualification of a bankruptcy judge is jurisdictional since his jurisdiction can in no event exceed that of the district court from which the bankruptcy judges' authority has been referred.

(d) The Petitioners Were Not Given a Full Opportunity to Develop Information Relating to the Scope of the Knowledge of the Bankruptcy Judge.

The Petitioners' Motion to Vacate was accompanied by copies of the transcript of the telephone conversation wherein the judge first revealed his stock ownership, the *Value Line* on J.P. Morgan and the judge's Financial Disclosure Reports. App.-18 and 22 for transcript and *Value Line*.

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[36] Decisions by courts without jurisdiction over the subject matter are void and may be collaterally attacked except where the issue of subject matter jurisdiction has been litigated in which case it must be raised by appeal. *Stoll v. Gottlieb*, 305 U.S. 165 (1938).

The ownership of the stock and the relation of J.P. Morgan to Morgan Guaranty were not disputed. The Petitioners contended that this was sufficient to show the judge's disqualification at the times the Bankruptcy Court Orders were entered and that their invalidity legally followed. Alternatively, Petitioners requested the district court to provide them an opportunity to conduct discovery on the judge's interest and his knowledge of that interest.

The bankruptcy judge informed the parties of his interest on March 23, 1987. Petitioners filed their motion on March 31, 1987, and about April 1, 1987, caused notices to be issued to take the bankruptcy judge's deposition. Other efforts to examine the scope of the judge's interest and knowledge were also undertaken. See App.-26 for example of other steps being taken.

The district judge not only relied on the undisputed fact of ownership, but drew numerous factual, exculpatory inferences from the unsworn information and denied any opportunity to conduct discovery, put on evidence, or be heard on the facts.[37] For example, the district court "found" that the judge consulted a "knowledgeable professional" about the connection between J.P. Morgan and Morgan Guaranty and was told there was no connection. App.-13. The unsworn record does not even reflect who this knowledgeable professional is, but it does show that this person does not recall the conversation described. *Id.* Customary inquiry would reveal how a "knowledgeable professional" could not know of the relation between J.P. Morgan and Morgan Guaranty and whether the conversation recalled by the bankruptcy judge was with his broker, someone else, or was only an intended

[37] A status conference was held before the district judge concerning jurisdiction and timing of the decision.

inquiry memory of which later was merged with reality. Deposition testimony would reveal the full scope of information in the judge's possession, e.g., fiduciary and personal tax information on dividends, other reports received, reports from brokers, etc. All of this is pertinent if the admitted ownership of the stock and possession of the *Value Line* information is not legally sufficient to show disqualification under § 455(b)(4) or § 455(a). Petitioners believe that it was, but were willing to develop further information in case, applying an objective standard, the court wanted more information. Nevertheless, the district court entered the Order Quashing Deposition.[38]

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[38] The Petitioners had also noticed the bankruptcy judge's deposition from the clerk's office of the Bankruptcy Court. This notice was subsequently suspended indefinitely by the newly assigned bankruptcy judge. App.-33.

CONCLUSION

For the foregoing reasons, Petitioners believe this case presents serious issues of the administration of the federal bankruptcy courts and the proper procedures required to protect the appearance of impartiality of bankruptcy judges. For this cause, Petitioners urge this Court to issue a writ of certiorari to the United States Court of Appeals for the Fifth Circuit to review its decision herein.

Respectfully submitted,

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87-846

No. _____

Supreme Court, U.S.
FILED
NOV 21 1987
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A.T. DAVIS, A.T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A.T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T.C. DAVIS, II, T. C. DAVIS, II TRUST, T.C. DAVIS, II TRUST "A", T.C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T.C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.

Respondents

APPENDIX TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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EDITOR'S NOTE

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PETITIONERS' APPENDIX

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28 U.S.C. § 455 (1982)

DISQUALIFICATION OF JUSTICE, JUDGE, OR MAGISTRATE

(a) Any justice, judge, or magistrate of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

(b) He shall also disqualify himself in the following circumstances:

(1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

(2) Where in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it;

(3) Where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy;

(4) He knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding;

(5) He or his spouse, or a person within the third degree of relationship to either of them, or the spouse of such a person:

(i) Is a party to the proceeding, or an officer, director, or trustee of a party;

(ii) Is acting as a lawyer in the proceeding;

(iii) Is known by the judge to have an interest that could be substantially affected by the outcome of the proceeding;

(iv) Is to the judge's knowledge likely to be a material witness in the proceeding.

(c) A judge should inform himself about his personal and fiduciary financial interests, and make a reasonable effort to inform himself about the personal financial interests of his spouse and minor children residing in his household.

(d) For the purposes of this section the following words or phrases shall have the meaning indicated:

(1) "proceeding" includes pretrial, trial, appellate review, or other stages of litigation;

(2) the degree of relationship is calculated according to the civil law system;

(3) "fiduciary" includes such relationships as executor, administrator, trustee, and guardian;

(4) "financial interest" means ownership of a legal or equitable interest, however small, or a relationship as a director, adviser, or other active participant in the affairs of a party, except that:

(i) Ownership is a mutual or common investment fund that holds securities is not a "financial interest"

in such securities unless the judge participates in the management of the fund;

(ii) An office in an educational, religious, charitable, fraternal, or civic organization is not a "financial interest" in securities held by the organization;

(iii) The proprietary interest of a policyholder in a mutual insurance company, of a depositor in a mutual savings association, or a similar proprietary interest, is a "financial interest" in the organization only if the outcome of the proceeding could substantially affect the value of the interest;

(iv) Ownership of government securities is a "financial interest" in the issuer only if the outcome of the proceeding could substantially affect the value of the securities.

(e) No justice, judge, or magistrate shall accept from the parties to the proceeding a waiver of any ground for disqualification enumerated in subsection (b). Where the ground for disqualification arises only under subsection (a), waiver may be accepted provided it is preceded by a full disclosure on the record of the basis for disqualification.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 87-1251

In The Matter Of:

KENDAVIS HOLDING COMPANY, et al., Debtors.

KENDAVIS HOLDING COMPANY, et al.,
Plaintiffs-Appellants,

versus

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC., and LOFFLAND BROTHERS CO.,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Texas (CA3-86-2995"G")

(September 24, 1987)

Before BROWN, GARZA and REAVLEY, Circuit Judges.

Per Curiam:*

* Local Rule 47.5 provides: "The publication of opinions that have no precedential value and merely decide particular cases on the basis of well-settled principles of law imposes needless expense on the public and burdens on the legal profession." Pursuant to that Rule, the court has determined that this opinion should not be published.

The court can find no merit in this appeal. Former stockholders in an insolvent debtor corporation and former management of that corporation, claiming rights of representation of creditors that can now be fully paid, want

to vacate a plan of reorganization that has been substantially implemented. The one aspect of the appeal that is not frivolous is the contention that the bankruptcy judge who confirmed the plan was disqualified under 28 U.S.C. § 455. Under some circumstances that issue would deserve an evidentiary hearing before the district court, but under the circumstances of this case the district judge was entitled to accept the bankruptcy judge's statement of his lack of knowledge that the corporation in which he held stock was the corporate parent of a creditor of the bankrupt debtor and might be affected by the outcome of the proceeding. The record does not justify questioning the bankruptcy judge's assurance. Furthermore, we think it clear that the bankruptcy judge's impartiality could not reasonably be questioned.

The record shows that the original bankruptcy judge immediately removed himself from the case when he found that a corporation in which he owned a very small share of the stock was a corporate parent of a creditor. Orders have been issued by another bankruptcy judge, and steps have been taken by the corporate successor to the debtor, implementing the plan. An evidentiary hearing could only add needless expense and delay the necessary continuation of the plan.

To avoid any doubt on the character of our holding we make clear that, disregarding the contentions or holdings by the district court on standing, this court has examined and determined all issues on their intrinsic merits or lack thereof.

AFFIRMED.

Filed in The U.S. Court of Appeals on September 30, 1987

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 87-1251

In The Matter Of:

KENDAVIS HOLDING CO., et al.,
Plaintiffs-Appellants,

versus

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING CO., KENDAVIS INDUSTRIES INTERNATIONAL, INC., and LOFFLAND BROTHERS CO.,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Texas

CERTIFICATE

I certify that because of the emergency created by recusals of assigned judges and the unavailability of active judges of the Fifth Circuit to serve on the panel assigned to hear this case, it was necessary to constitute the panel with two senior judges of this circuit.

Witness my signature this 16th day of September 1987.

/s/ CHARLES CLARK
Chief Judge

UNITED STATES COURT OF APPEALS
FIFTH CIRCUIT

Office Of The Clerk

GILBERT F. GANUCHEAU
Clerk

Tel. 504-589-6514
600 Camp Street
New Orleans, LA 70130

July 15, 1987

TO COUNSEL LISTED BELOW:
No. 87-1251 — In Re: Kendavis Holding Co.

Dear Counsel:

The Court regrets to advise that it now appears that all members of the panel which heard argument in the above matter on June 3, 1987 are recused. Therefore, the submission of this case for decision to that panel has been vacated.

The case has now been scheduled to be re-argued before a different panel of judges who will not be disqualified, on Wednesday, September 16, 1987 at 9:00 a.m. in the East Courtroom, Room 223 of the U. S. Court of Appeals Building, 600 Camp Street, New Orleans, Louisiana. The Court will allow a period of 30 minutes to the side. Counsel are requested to acknowledge receipt on the enclosed acknowledgment form.

Counsel for FDIC is being informed that their letter of June 1, 1987, that the FDIC will not offer oral argument but join in and adopt the argument offered by appellee Official Unsecured Creditors Committee, has been sent to the new panel members. If this will not be the situation for the next argument, counsel should so inform this office.

Very truly yours,

/s/

GILBERT F. GANUCHEAU
Clerk

GFG/jmg
Enclosure

Ms. Barbara J. Houser
Mr. Richard E. Coulson
Mr. J. Lyndell Kirkley
Mr. David C. Heiman
Mr. Joseph U. Schorer
Mr. J. Maxwell Tucker
Mr. Stephen A. Goodwin
Mr. Jerry Beane
Mr. George J. Wade

Filed in the U.S. District Court,
Northern District of Texas on
April 10, 1987

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

In Re: KENDAVIS HOLDING COMPANY, et al., *Debtors/Appellants.*	CIVIL ACTION NO. CA 3-86-2995-G

MEMORANDUM ORDER

This case is before the court on appellants' motion to vacate and set aside the following rulings and orders of the Bankruptcy Court:

1. November 14, 1986 letter ruling;
2. November 24, 1986 order confirming the Official Unsecured Creditors Committees' Modified Joint Plan of Reorganization as to Kendavis Holding Company and Kendavis Industries International, Inc. (and related findings of fact, rulings, and conclusions of law);
3. August 6, 1986 order denying confirmation of the Debtors' Third Amended Joint Plan of Reorganization (and related findings of fact, rulings, and conclusions of law); and
4. November 24, 1986 order denying Debtors' motion for new trial.

The motion is made under Rule 60(b)(4) of the Federal Rules of Civil Procedure, as incorporated into Bankruptcy Rule 9024. Although not cast in the form of an appeal, the

motion is brought here because this court has jurisdiction over the orders in question until an appeal is taken from this court's rulings dated March 26, 1987.[1] The movants are parties to the prior bankruptcy proceedings.

For the reasons set forth in this court's memorandum orders and orders of March 26, 1987, the court remains convinced that appellants lack standing to appeal the confirmation of the Committees' plan and that the denial of confirmation of the Debtors' plan was not clearly erroneous. Thus, it is arguable that appellants lack standing to make this motion to vacate. Even assuming that appellants do have standing, however, this court is of the opinion that the motion to vacate should be DENIED.

Appellants base their motion to vacate on three grounds:

1. The orders in question are null and void because those orders were entered by a judge disqualified under 28 U.S.C. § 455(b)(4);
2. The orders in question are null and void because those orders were entered by a judge disqualified under 28 U.S.C. § 455(a); and
3. The appellants and all interested parties were deprived of their constitutional right to due process because Judge McGuire had a financial interest in a party to the bankruptcy cases.

---

[1] Notice of appeal from those rulings was given April 9, 1987. Under the general rule of this circuit, this court would ordinarily lose power, after such a notice, to take any further action except in aid of the appeal or to correct clerical errors. Nicol v. Gulf Fleet Supply Vessels, Inc., 743 F.2d 298, 299 (5th Cir. 1984). *Harcon Barge* requires, however, that this motion to vacate be deemed to have been brought under Rule 59. Harcon Barge Co., Inc. v. D & G Boat Rentals Inc., 784 F.2d 665, 667 (5th Cir.) (en banc), *cert. denied*, 107 S.Ct. 398 (1986).

The facts giving rise to the instant motion are as follows. Shortly after bankruptcy judge Robert C. McGuire was assigned the Kendavis cases in 1985, he learned that a bank named "Morgan" was involved. Individually and as trustee of two trusts under his mother's will, Judge McGuire held stock in J.P. Morgan & Co. Incorporated. He therefore called his broker to determine if there was any connection. Judge McGuire's recollection is that the broker told him that J.P. Morgan & Co. Incorporated and Morgan Guaranty Trust Company were separate companies and not connected.

Judge McGuire receives the Value Line Stock Reporting Services ("Value Line"). On the night of March 22, 1987, he noticed for the first time, while reading Value Line, that J.P. Morgan & Co. Incorporated, the company in which he held stock, owned Morgan Guaranty Trust Company of New York, a creditor in these cases. Although Judge McGuire felt certain that Value Line had set forth this information in its report every three months for the last three years, he had never noticed it until the night of March 22, 1987.

Judge McGuire called his broker the following day. The broker did not remember the earlier conversation, but told Judge McGuire that "if [Judge McGuire] said it took place, he's sure it did." Transcript of Proceedings, March 23, 1987, p. 4. The broker confirmed the information in Value Line to Judge McGuire. Later that same day, Judge McGuire notified counsel for the parties of the above facts. His most recent financial disclosure report reveals that he owns 808 shares of J.P. Morgan & Co. Incorporated. On March 26, 1987, Judge McGuire recused himself.

Appellants urge that their motion to vacate should be granted because the orders in question were entered by a bankruptcy judge disqualified under 28 U.S.C. § 455(b)(4). § 455(b)(4) provides, in pertinent part, that a judge shall

disqualify himself when he knows "that he, individually or as a fiduciary, . . . has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding." 28 U.S.C. § 455(b)(4).

By its own terms, § 455(b)(4) requires the judge to have knowledge of the interest. There is no "constructive knowledge" under § 455(b)(4). *See* Health Services Acquisition Corporation v. Liljeberg, 796 F.2d 796, 802 (5th Cir. 1986), *cert. granted*, 107 S.Ct. 1368 (1987). A judge who learns that he has a financial or other interest in a case is generally required only to recuse himself from future proceedings. *Health Services Acquisition Corporation v. Liljeberg, supra*, 796 F.2d at 801. Absent prior knowledge, the orders of a disqualified judge entered before acquiring knowledge remain valid under § 455(b)(4).

This court is persuaded that Judge McGuire did not have actual prior knowledge of his financial interest. He has fulfilled the requirements of § 455(b)(4) by his prospective recusal when he first learned of the disqualifying interest. It is thus unnecessary to vacate the rulings made by Judge McGuire prior to March 23, 1987.

Appellants also urge that their motion to vacate should be granted because the orders in question were entered by a judge disqualified under 28 U.S.C. § 455(a). In pertinent part, § 455(a) provides that any "judge . . . of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned." 28 U.S.C. § 455(a).

Rather than explicitly requiring knowledge, § 455(a) establishes an objective test which looks to whether "the reasonable man, were he to know all the circumstances, would harbor doubts about the judge's impartiality." *Health Services Acquisition Corporation v. Liljeberg, supra*, 796 F.2d at 800,

citing Potashnick v. Port City Construction Company, 609 F.2d 1101, 1111 (5th Cir.), *cert. denied*, 449 U.S. 820 (1980). The court in *Health Services* took an expansive view of the reasonable man standard, holding that recusal is required under § 455(a) even when a judge lacks actual knowledge of the facts indicating his interest or bias in the case, if a reasonable person, knowing all the circumstances, would expect that the judge would have actual knowledge (i.e., constructive knowledge). *Health Services Acquisition Corporation v. Liljeberg, supra*, 796 F.2d at 802. The court cautioned, however, that

> because of the harsh consequences that can result, knowledge of facts requiring recusal should not be lightly imputed to a judge. Where a reasonable person would only speculate that a judge might have actual knowledge of the facts, constructive knowledge does not exist.

Health Services Acquisition Corporation v. Liljeberg, supra, 796 F.2d at 803.

The facts in *Health Services* are a far cry from those in this case. Unlike the trial judge in *Health Services*, Judge McGuire never knew of the connection between J.P. Morgan and Morgan Guaranty until after he entered the orders in question. Before proceeding in the Kendavis cases, Judge McGuire asked a knowledgeable professional whether a relationship existed between Morgan Guaranty and J.P. Morgan and was told that it did not. Thus, there would have been no reason for Judge McGuire to review anything he received, such as Value Line, to determine whether any such relationship existed.

This court is of the opinion that a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual or constructive knowledge of

any conflict. Judge McGuire's previous rulings in the Kendavis cases thus should stand. Davis v. Xerox, Case No. 85-6285, slip op. (9th Cir. March 3, 1987) at 7-8; *Health Services Acquisition Corporation v. Liljeberg, supra*, 796 F.2d at 803.

Finally, the appellants urge their motion to vacate on due process grounds. A fair trial in a fair tribunal is a basic requirement of due process. In re Murchison, 349 U.S. 133, 136 (1955). Due process is denied when the judge has a direct, personal, substantial pecuniary interest in reaching a conclusion against a party in the case. Tumey v. State of Ohio, 273 U.S. 510, 523 (1927). *See also* Aetna Life Insurance Co. v. Lavoie, _____ U.S. _____, 106 S.Ct. 1580, 1584, 1589 (1986). The constitutional guarantee of due process is independent of the rights conferred by § 455. Yet, it was to protect this guarantee that the recusal statutes were enacted. 13A Wright, Miller & Cooper, FEDERAL PRACTICE AND PROCEDURE, § 3541, at 550 n. 6 (1984). It would be anomalous to hold that a claim under the statutes insufficient on its merits could nevertheless satisfy constitutional standards. In re International Business Machines Corporation, 475 F.Supp. 1372, 1390 (S.D.N.Y. 1979), *aff'd*, 618 F.2d 923, 932 n. 11 (2d Cir. 1980).

The record reflects that the shares held by Judge McGuire consistently represented only .00023% approximately of J.P. Morgan's common stock. Given the court's previously announced conclusion that the facts in this case do not warrant retrospective recusal under the relevant statutes, §§ 455(a) or (b)(4), it would be similarly anomalous to hold that appellants satisfied the constitutional, but not statutory, standards.

For the foregoing reasons, the appellants' motion to vacate is **DENIED.**

SO ORDERED.

April 10, 1987.

/s/ A. JOE FISH
A. Joe Fish
United States District Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

In Re:

KENDAVIS HOLDING COMPANY,
KENDAVIS INDUSTRIES
INTERNATIONAL, INC.,
LOFFLAND BROTHERS COMPANY
MID-CONTINENT SUPPLY CO.,
GEODRIL, INC.
LOFFLAND BROTHERS EASTERN
HEMISPHERE, INC., and
LOFFLAND BROTHERS
(SINGAPORE) PTE., LTD.,

Debtors

Case No. 385-30348-M-11

• • • • • • • • • • • • • •

TRANSCRIPT OF PROCEEDINGS

• • • • • • • • • • • • • •

BE IT REMEMBERED THAT on the 23 day of March, 1987, before the Honorable Robert C. McGuire, United States Bankruptcy Judge, at Dallas, Texas, the above-styled and numbered cause came on for Hearing and the following constitutes the Transcript of such proceeding as hereinafter shown:

P-R-O-C-E-E-D-I-N-G-S

THE COURT: You all there?

MR. FLOWERS: Yes, we are. Flowers and Houser are here, Judge.

MR. BLINN: We have Goodwin and Blinn.

THE COURT: Something came to my attention last night that I think you all need to be aware of. I felt that communication with you two as representatives of the remaining diverse groups would be sufficient notice initially, and I'm having this conference reported.

When I first got into the Kendavis cases and became aware there was a bank named Morgan involved it, I called my broker because individually and as Trustee of two trusts, my brothers, under my mother's will, I held stock interest in J.P. Morgan Company.

My recollection is that the broker told me the J.P. Morgan Company and Morgan Guaranty were separate companies and aren't connected. I get the Value Line Stock Reporting Services, and every three months they report on the companies they cover. Last night for the first time I noticed in reading the discussion on J.P. Morgan Company, Inc., that it stated that J.P. Morgan Company owns Morgan Guaranty Trust Company of New York. I'm sure that it has had this statement in there on every three month's report for the last three years, but I never noticed it until last night.

Except for stock splits on the stock in 1985 and 1987, my ownership in the stock has not changed and there have been no trades or sales by me of it. The stock interest is not a diminimus amount. When I called the broker today he said he didn't remember the conversation, but if I said it took place, he's sure it did. Frankly, I wish his memory was better but the facts are what they are. He also today confirmed the information in Value Line.

Under the circumstances, and if in truth and in fact J.P. Morgan Co., Inc. does own Morgan Guaranty Trust Company of New York, which it appears that it does, then it appears that I should recuse myself from further consideration of these cases. I have not talked to Judge Abramson yet about

taking them on since this matter just came to my attention, and I realize that this is just coming to your attention and you may want to evaluate it before making any comment.

I'm going to be in Wichita Falls Tuesday and Wednesday of this week. It appears to me that perhaps a starting point would be for you to check with Mr. Lewis regarding the relationship of the banks, although, apparently, there's not much question about it. Also, I would be willing to immediately dispose of the J.P. Morgan stock and continue in the case, but I think that puts the attorneys and clients in an uncomfortable position for a number of reasons. In a case on another occasion where recusal was not really involved, I followed a procedure which I had heard recommended elsewhere, and that was to give the attorney a certain period of time to call my secretary without identifying themselves to advise if they preferred me to recuse myself. If the call was received, then I would sign the order of recusal; if not, then I would remain in the case. In this instance, I can, if the facts on Morgan are as they appear to be, recuse myself and or follow the procedure indicated, and if no calls were received, sell the stock and remain in the case.

I realize that this is hitting you all out of the blue, as it did me, and since I will be out of town Tuesday and Wednesday, I would suggest we set up a time now for you to come in either on Thursday or Friday for a brief status conference. The status conference would not discuss the merits at all. It would just be for the purpose of disposing of this issue or setting up a procedure for disposing it.

Additionally, in the interim, I will have the opportunity to discuss it with Judge Abramson. The statute involved is 28 U.S.C., Section 455. This particular basis for recusal cannot be waived by the parties. The only issue is whether ownership in a parent is ownership of a subsidiary for purposes of Section

455; however, I think that perhaps is a nonissue. My suggestion is, and I'm not asking for any of your comments at this time unless you think they're appropriate, to perhaps either Thursday or Friday morning maybe we could have a meeting at 8:30 and you give me whatever thoughts you want to give me on it. Does either side have any comment they wish to make?

MR. FLOWERS: Judge, the 8:30 time on Thursday would be fine with us.

MR. BLINN: This is John Blinn. That's fine with us as well, Judge.

THE COURT: Unless somebody wants to say something, why don't we plan to meet at 8:30 on Thursday morning then.

MR. FLOWERS: Fine.

MR. FLOWERS: Thank you.

THE COURT: Okay. See you then.

CERTIFICATION

I, DARLA M. CHAVEZ, certify that during the proceedings in the foregoing styled and numbered cause, I was the official Court Reporter and took in stenograph notes such proceedings and have transcribed the same as shown by the above and foregoing ____ pages, and that said transcript is true and correct.

This the ____ day of _____, 1987.

_____

U.S. BANKRUPTCY COURT REPORTER
THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

March 20, 1987

THE VALUE LINE Investment Survey

Part 1 Summary & Index

File at the front of the Ratings & Reports binder. Last week's Summary & Index should be removed.

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The Median of Estimated **PRICE-EARNINGS RATIOS** of all stocks with earnings

16.9

26 Weeks Ago*	Market Low 12-23-74*	Market High 12-13-68*
14.7	4.8	19.0

The Median of **ESTIMATED YIELDS** (next 12 months) of all dividend paying stocks under review

2.4%

26 Weeks Ago*	Market Low 12-23-74*	Market High 12-13-68*
2.7%	7.8%	2.7%

The Estimated Median **APPRECIATION POTENTIAL** of all 1700 stocks in the hypothesized Economic environment 3 to 5 years hence

40%

26 Weeks Ago*	Market Low 12-23-74*	Market High 12-13-68*
55%	234%	18%

*Estimated medians as published in *The Value Line Investment Survey* on the dates shown.

ANALYSES OF INDUSTRIES IN ALPHABETICAL ORDER WITH PAGE NUMBER

Numeral in parenthesis after the industry is rank for probable performance (next 12 months).

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Air Transport (12)	251	Drug (8)	1250	Japanese Diversified (75)	1580	Railroad (61)	300
Aluminum (66)	1217	Drugstore (86)	786	Machinery (41)	1301	Real Estate (82)	668
Apparel (22)	1601	Electrical Equipment (47)	1001	Machinery (Const. & Mng.)(67)	1356	R.E.I.T. (74)	1189
Auto & Truck (29)	101	Electric Utility (Central) (81)	701	Machine Tool (78)	1344	Recreation (63)	1751
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*Reviewed in this week's edition

In three parts: This is Part I, the Summary & Index. Part II is Selection & Opinion. Part III is Ratings & Reports. Volume XLII, No. 26.

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NAME OF STOCK	Ticker Symbol	Recent Price	Timeliness	Safety	Beta	Estimated Range of 3-5 yr. average prices 1990-91	Current P/E Ratio	Est'd Yield Next 12 mos.	Est'd Earns. 12 mos. to 6-30-87	(f) Est'd Div'd next 12 mos.	Industry Rank	LATEST RESULTS Qtr. Ended	Earns. Per sh.	Year Ago	Technical Rank Qtr. Ended	Latest Div'd	Year Ago	Where Options Trade
874 1895 Milepore Corp (OTC)	MILI	42	1	3	1.15	50- 75 (20- 80%)	27.1	0.8%	1.55	.34	10	12/31	.46	.36	6/30	.07	.06	3
189 Miller, Roy	MRC	13	3	3	1.00	18- 25 (40- 90%)	37.1	3.4%	.35	.44	39	12/31	.08	d.05	3/31	.11	.11	4
1439 1897 Minnesota Mining	MMM	125	3	1	1.10	140- 175 (10- 40%)	17.0	3.6%	7.35	3.72	10	12/31	1.83	1.53	3/31	▲.93	.90	2 CBO
731 Minnesota Power & Li	MPL	29	2	2	.75	30- 45 (5- 55%)	10.9	5.7%	2.90	1.66	81	12/31	.44	.38	3/31	▲.415	.38	2
484 Mitchell Energy & Dev (ASE)	MND	14	3	4	1.15	14- 20 (0- 45%)	88.7	1.7%	.21	.24	58	1/31	♦.03	.29	6/30	.06	.06	3 PAC
773 Mitel Corp	MLT	5¾	3	5	1.20	8- 15 (40-160%)	NMF	NIL	d.58	NIL (h)	66	11/30	d.02(b)	d.69(b)	12/31	NIL(b)	NIL(b)	3
413 Mobil Corp	MOB	44	3	2	.95	40- 60 (N- 35%)	14.3	5.8%	3.07	2.20	51	12/31	.74	1.20	3/31	.55	.55	1 CBO
774 Mobile Communic 'B' (OTC)	MCCAB	26	3	4	1.10	25- 40 (N- 53%)	70.3	NIL	.37	NIL	66	9/30	.07	.08	12/31	NIL	NIL	1
888 Modine Mfg (OTC)	MODI	31	3	3	.75	35- 50 (15- 60%)	10.7	2.5%	2.89	.76	83	12/31	.86	.56	3/31	.19	.17	3
1571 923 Mohasco Corp	MOH	36	3	3	.95	35- 50 (N- 40%)	17.2	1.8%	2.09	.36	32	12/31	.75	.76	3/31	.09	.08	3
1194 Monarch Data Sciences	MOS	2⅞	3	5	1.35	5- 9 (100-260%)	8.1	NIL	.31	NIL	7	1/31	.07	d.33	3/31	NIL	NIL	3
1840 Molex Inc (e) (OTC)	MOLX	43	2	3	1.05	45- 65 (5- 50%)	25.3	0.1%	1.70	.03	56	12/31	.38	.29	3/31	.007	.005	3
1545 Molson Cos Ltd A (TSE)	MOLA TO	25 (b)	3	2	.65	30- 45 (20- 80%)	12.4	3.2%	2.01	.80	16	12/31	.50(b)	.30(b)	3/31	.20 (b)	.20 (b)	4
1449 1294 Monarch Capital Corp	MON	80	2	3	.95	95- 140 (5- 80%)	16.8	NIL	5.43	NIL	57	12/31	1.83	1.21	3/31	NIL	NIL	3
1398 Monarch Mach. Tool	MMO	17	3	3	.95	20- 25 (20- 45%)	63.0	4.7%	.27	80-NIL	78	12/31	.17	.26	3/31	.20	.20	4
1894 1495 Monfort of Colorado (OTC)	MNFT	79	–	3	.55	45- 65 (N- N%)	12.8	1.1%	5.99	.90	38	11/30	1.43	1.37	3/31	.90	NIL	4
1672 Monolithic Memories (OTC)	MMIC	15	3	4	1.55	18- 30 (20-100%)	28.8	NIL	.52	NIL	77	12/31	.08	.02	3/31	NIL	NIL	3 PAC
1141 1246 Monsanto	MTC	78	3	3	1.10	110- 165 (40-110%)	15.2	3.5%	5.12	2.75	18	12/31	.58	d.36	3/31	.65	.575	2 CBO
1728 Montana Power	MTP	40	3	3	.80	40- 55 (0- 40%)	12.5	6.8%	3.21	2.71	80	12/31	1.13	.58	3/31	▲.67	.60	3
2104 Montgomery St Inc Sec	MTS	22	3	1	.55	20- 25 (N- 15%)	NMF	9.1%	NMF	2.00	33	6/30	19.75(q)	18.52(q)	9/30	.47	.48	3
1178 MONY Real Estate Inv	MYM	9¼	3	2	.75	12- 17 (30- 85%)	12.4	7.7%	.75	72- .88	74	11/30	.14	.20	3/31	.22	.22	3
671 Moog Inc 'A' (ASE)	MOG.A	16	4	4	1.35	20- 35 (25-120%)	13.1	1.8%	1.22	.28	69	12/31	.11	.25	6/30	.07	.07	3
1125 Moore Corp	MCL	24	5	1	.85	20- 30 (N- 25%)	16.0	3.1%	1.50	.74	52	12/31	.44	.46	6/30	.18	.18	4
888 Moore McCormack Res	MMR	24	3	3	1.00	30- 50 (25-110%)	21.1	2.2%	1.14	.52	30	12/31	.35	.50	3/31	.13	.26	4
2026 Morgan (J.P.) & Co	JPM	48	3	1	1.10	60- 75 (30- 65%)	9.9	3.0%	4.67	1.40	21	12/31	1.02	.95	6/30	♦.34	.306	3 PHL
325 Morrison, Inc (OTC)	MORR	26	4	3	1.00	30- 45 (15- 75%)	17.9	1.8%	1.45	.48	84	11/30	.37	.37	3/31	.12	.114	3
876 Morrison Knudsen	MRN	52	4	1	.85	60- 70 (15- 35%)	13.3	2.9%	3.92	1.50	33	12/31	.99	1.21	3/31	.37	.74	3
1882 1674 Morse Shoe	MRS	39	–	3	1.00	35- 55 (N- 40%)	19.8	2.2%	1.97	.85	82	12/31	.59	.48	6/30	.20	.20	3
1179 Mortgage Growth Inv (ASE)	MTG	22	3	2	.80	25- 35 (15- 60%)	12.9	7.5%	1.71	1.65	74	11/30	.37	.36	3/31	.40	.40	2
1189 Mortgage & Rity Trust	MRT	22	3	3	.80	25- 35 (15- 60%)	12.8	8.6%	1.75	1.90	74	12/31	.42	.72	3/31	.47	.57	3
516 Morton Thiokol	MTI	48	3	3	1.00	50- 70 (5- 45%)	16.8	1.8%	2.90	.78	15	12/31	.88	.68	3/31	.19	.175	3 PHL
1673 Motorola, Inc	MOT	80	3	3	1.25	80- 85 (20- 70%)	28.8	1.3%	1.88	.64	77	12/31	.49	.37	6/30	.16	.16	3 ASE
382 Multimedia, Inc (OTC)	MMEDC	54	–	3	NMF	50- 80 (N- 50%)	NMF	NIL	d.03	NIL	71	9/30	d.01	.44	12/31	NIL	NIL	–
1510 Munford, Inc	MFD	19	5	3	.95	20- 35 (5- 85%)	38.0	2.8%	.48	.54	72	12/31	.28	.78	6/30	.135	.135	4
1810 Munsingwear	MUN	11	4	3	.80	20- 30 (80-175%)	22.9	NIL	.48	NIL	22	12/31	d.17	.10	3/31	NIL	NIL	4
414 Murphy Oil Corp	MUR	31	3	3	1.15	25- 40 (N- 30%)	NMF	2.4%	.16	.75	51	12/31	d.15	.49	3/31	.25	.25	1 PAC
891 1766 Murray Ohio Mfg	MYO	24	4	3	.85	25- 40 (5- 65%)	37.0	2.5%	.89	.60	83	12/31	d.54	d.03	6/30	.15	.30	4
2106 Mut I of Omaha Inv Sh	MUO	17	3	1	.80	15- 20 (N- 20%)	NMF	8.5%	NMF	1.44	33	6/30	14.04(q)	13.33(q)	6/30	.36	.36	3
1281 Mylan Labs	MYL	18	3	3	1.00	18- 30 (15- 90%)	33.5	0.8%	.58	.10	9	12/31	.15	.17	3/31	.05	.033	4 ASE
884 NBD Bancorp	NBD	36	2	1	1.00	35- 45 (0- 30%)	9.3	3.4%	3.75	1.20	34	12/31	1.03	.87	3/31	.30	.230	3
839 1126 NBI, Inc	NBI	10	4	4	1.35	17- 25 (70-150%)	NMF	NIL	d.50	NIL	52	12/31	d.43	NIL	3/31	NIL	NIL	3 CBO
517 NCH Corp	NCH	34	2	1	.70	45- 55 (30- 80%)	18.7	2.1%	2.04	.72	18	1/31	♦.51	.44	3/31	.18	.18	4
2037 NCNB Corp	NCB	25	3	2	1.00	35- 45 (40- 80%)	8.8	3.4%	2.55	.86	31	12/31	.58	.52	3/31	.21	.19	3
1186 NCR Corp	NCR	66	3	2	1.25	60- 85 (N- 30%)	18.1	1.5%	3.64	1.00	7	12/31	1.39	1.33	6/30	▲.25	.23	3 CBO
1587 NEC Corp (ADR) (OTC)	NIPNY	63	4	3	.85	50- 75 (N- 20%)	NMF	0.4%	.50	.25	75	9/30	.35(p)	.44(p)	12/31	.137	.111	1
340 1862 NL Inds	NL	9¾	–	4	NMF	8- 12 (40-105%)	NMF	3.4%	d2.22	20-NIL	80	9/30	d8.19	.07	6/30	.05	.05	– PHL
1439 485 NUI Corp	NUI	42	2	2	.80	35- 45 (N- 5%)	15.2	5.8%	2.77	2.36	70	12/31	1.20	.70	3/31	.58	.58	3
281 NWA Inc	NWA	71	2	3	1.15	80- 115 (15- 60%)	17.7	1.3%	4.01	.90	12	12/31	.48	d.09	3/31	.225	.225	3 CBO
1881 NACCO Inds A	NC	28	3	3	.70	30- 40 (5- 45%)	11.2	1.8%	2.49	.50	44	12/31	.85	.61	3/31	.125	.092	3
518 Nalco Chemical	NLC	33	3	3	1.00	35- 55 (5- 65%)	17.7	3.6%	1.86	1.20	15	12/31	.41	.47	3/31	.30	.30	3
1127 Nashua Corp	NSH	29	3	3	1.15	30- 45 (5- 55%)	13.8	1.8%	2.10	.30	52	12/31	.43	.51	6/30	.05	NIL	3
857 National City Corp (OTC)	NCTY	34	2	1	.85	35- 45 (5- 30%)	8.9	3.7%	3.42	1.25	34	12/31	1.29	.77	6/30	▲.30	.25	3
1128 National Computer (OTC)	NLCS	16	4	3	1.25	25- 40 (55-165%)	17.6	1.3%	.85	.20	52	10/31	.13	.20	6/30	.05	.04	4
1520 National Convenience Str	NCS	9⅝	5	4	1.05	10- 20 (5-110%)	NMF	3.8%	.10	36-NIL	72	12/31	d.02	d.02	6/30	.09	.09	4
2125 National Data Corp (OTC)	NDTA	25	2	3	1.10	30- 50 (20-100%)	30.8	1.8%	1.20	.44	1	11/30	.30	.24	3/31	.11	.11	3
1139 1888 National Distillers	DR	61	2	3	.85	65- 95 (5- 55%)	24.2	3.8%	2.52	2.20	10	12/31	.90	.53	3/31	.55	.55	2 ASE
1885 National Education	NEC	25	2	3	1.00	30- 50 (20-100%)	21.4	NIL	1.17	NIL	25	12/31	.42	.32	3/31	NIL	NIL	3
877 National Enterprises	NEI	5	3	5	1.50	6- 9 (20- 80%)	31.3	NIL	.16	NIL	39	12/31	d.02	d.23	12/31	NIL	NIL	5
486 National Fuel Gas	NFG	41	4	2	.65	40- 50 (N- 20%)	10.6	5.8%	3.85	2.38	70	12/31	1.16	1.23	6/30	♦.57	.52	2
1483 National Intergroup	NII	14	4	4	1.30	20- 30 (45-115%)	NMF	1.8%	d1.84	25- .16	58	12/31	d.40	d.67	6/30	.062	.062	4
1395 National Medical Enterpr	NME	28	3	3	1.40	50- 80 (80-185%)	15.1	2.3%	1.86	.64	68	11/30	.38	.49	3/31	.15	.14	3 ASE
232 National Patent Dev (ASE)	NPD	15	▼5	4	1.20	25- 40 (60-165%)	NMF	0.7%	d.60	.10	77	9/30	d.26	d.27	3/31	.025	.025	5 PAC
1741 142 National Presto Ind	NPK	33	4	1	.70	40- 50 (20- 50%)	14.5	3.9%	2.28	1.17	17	12/31	.70	.80	6/30	.285	.55	3
1874 National Semiconductor	NSM	15	3	4	1.50	14- 25 (N- 65%)	NMF	NIL	NIL	NIL	77	11/30	d.09	d.48	3/31	NIL	NIL	3 CBO
1494 National Service Ind	NSI	27	3	1	.75	25- 35 (N- 30%)	11.3	2.4%	1.51	.64	58	11/30	.37	.35	3/31	▲.16	.137	4
837 1325 National Standard Co	NSD	13	4	3	.75	15- 20 (15- 55%)	NMF	3.1%	d1.19	40-NIL	41	12/31	d1.23	.45	3/31	.10	.10	4
189 Navistar Int'l	NAV	6⅞	4	5	1.00	7- 13 (0- 90%)	NMF	NIL	NIL	NIL	29	1/31	.02	.08	12/31	NIL	NIL	4
1391 819 Neutrogena Corp (e) (OTC)	NGNA	34	▲1	3	.45	25- 40 (N- 20%)	49.3	0.4%	.69	.12	11	1/31	♦.30	.17	12/31	NIL	NIL	3
1721 Nevada Power	NVP	21	3	2	.60	25- 30 (20- 45%)	11.9	7.0%	1.76	1.46	80	12/31	.26	.16	3/31	.36	.355	3
883 Newell Co	NWL	36	3	3	.95	40- 60 (10- 65%)	14.8	2.3%	2.42	.84	43	12/31	.84	.61	3/31	.21	.175	4
1436 New England Bus (OTC)	NEBS	24	3	2	.55	35- 50 (45-110%)	21.8	2.0%	1.10	.48	–	12/31	.25	.23	3/31	▲.12	.04	3
195 New England Elec	NES	29	3	2	.70	30- 35 (5- 20%)	8.9	6.9%	3.27	2.00	80	12/31	.83	.67	6/30	.50	.48	2
877 Newhall Land & Farming	NHL	36	3	3	.80	40- 60 (10- 65%)	15.4	2.5%	2.34	.90	82	12/31	.71	.53	3/31	.20	.10	4
★ ★ 234 Newmont Mining	NEM	85	2	3	1.05	95- 145 (10- 70%)	30.5	1.2%	2.79	1.00	13	12/31	.30	d.18	3/31	.25	.25	1 PHL
160 Newport Corp (OTC)	NEWP	16	4	3	1.30	25- 35 (55-120%)	24.6	0.4%	.65	.06	38	1/31	.11	.13	12/31	.03	.03	5
1290 1702 New Process (ASE)	NOZ	31	3	3	.95	25- 40 (N- 30%)	15.5	3.8%	2.00	1.18	46	12/31	.71	.71	3/31	.805	.875	3
1786 New World Pictures (ASE)	NWP	13	–	5	NMF	16- 30 (25-130%)	15.5	NIL	.84	NIL	63	9/30	.13	.05	3/31	NIL	NIL	–
198 N.Y. State Elec. & Gas	NGE	28	3	3	.85	30- 50 (5- 80%)	7.3	9.6%	3.85	2.68	80	12/31	.79	.68	3/31	.66	.64	3
1818 N.Y. Times (ASE)	NYTA	45	2	3	1.10	50- 75 (10- 65%)	24.9	0.9%	1.81	.40	6	12/31	.43	.36	6/30	.09	.075	3 PAC
197 Niagara Mohawk	NMK	17	5	4	.80	25- 35 (45-105%)	8.4	12.2%	2.66	2.08 1.42	80	12/31	.58	.58	3/31	.52	.52	4 ASE

(c) Dividends estimated partly exempt from ordinary income tax.
d Deficit
(e) Includes distribution of assets.
(f) The estimate may reflect a probable increase or decrease. If a dividend boost or cut is possible but not probable, two figures are shown: the first is the most likely.
(g) Dividends subject to foreign withholding tax for U.S. residents.
(h) Est'd Earnings & Est'd Dividends after conversion to U.S. Dollars at Value Line estimated translation rate.
(j) Trading suspended.
(k) 12 months (m) 9 months (p) 6 months
(q) Asset value (r) Estimates
(s) Rank removed due to outstanding exchange offer
(u) Excludes distribution of assets.
N Negative figure NA Not available
NC Not comparable NMF No meaningful figure

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THE VALUE LINE Investment Survey

Part 3 Ratings & Reports

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Pages 2000—2142

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★★Rank highest for Timeliness
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ESPECIALLY NOTEWORTHY:

We welcome four new companies to this week's Edition. ***Branch Corp.*** *(page 2010),* ***First Alabama Bankshares*** *(page 2020), and* ***Meridian Bancorp.*** *(page 2034) have been deposited in the Bank Industry, while* ***Comp-U-Card*** *(page 2061) has been hooked up to the Financial Services Industry.*

Cyclops *has recently received some eye-popping attention. Read about this take-over odyssey on page 2113.*

Now that it has avoided ***First Interstate's*** *amorous embrace,* ***Bank-America*** *can resume its search for profitability. Pages 2022 and 2003.*

NCNB's *Chilean loans proved far too spicy for management's taste. Are more portfolio sales likely? Our answer is on page 2037.*

Midlantic Banks has decided that its enhanced operations deserve a new name. Hence, ***Midlantic Corp.,*** *which can now be found on page 2035.*

Lomas & Nettleton *is charging into the credit card business. See page 2070.*

Investors need to be swift-of-foot to keep pace with ***Fleet's*** *rapid growth. Turn to page 2027 for more.*

Sallie Mae *is still winning hearts on Wall Street. Page 2073.*

Bank of New England *is sprouting branches throughout Massachusetts, thanks to its acquisition of Conifer. Our analysis is rooted on page 2006.*

Will any of ***Lotus'*** *leaves be picked by Microsoft? Return to page 2124 for a printout of the situation.*

In three parts: Part I is the Summary & Index. Part II is Selection & Opinion. This is Part III, Ratings & Reports. Volume XLII, No. 26.

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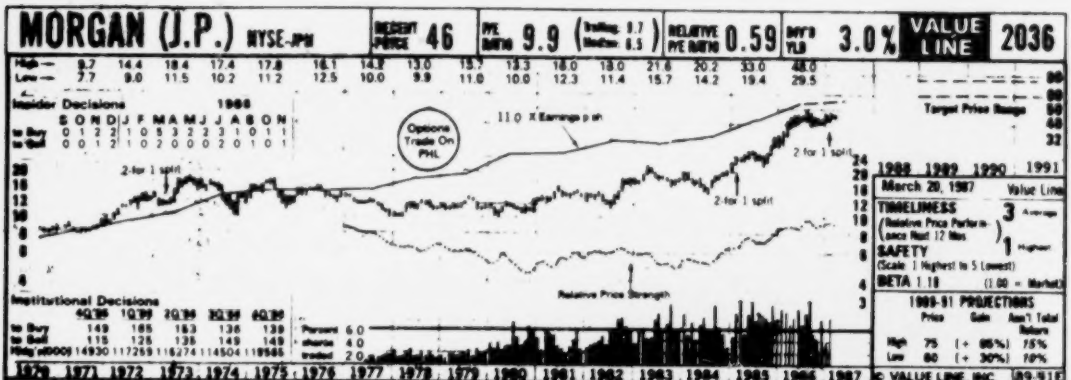

1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	© VALUE LINE, INC.	89-91
70	75	82	97	1.17	1.24	1.26	1.34	1.64	1.77	2.24	2.27	2.67	2.63	2.94	3.91	4.74	5.10	Earnings per sh (A)	6.25
.31	.34	.35	.37	.41	.45	.46	.51	.57	.64	.72	.79	.87	.94	1.03	1.13	1.26	1.40	Div'ds Decl'd per share	1.85
5.13	5.57	6.02	6.53	7.14	8.31	8.40	10.29	11.38	12.80	14.09	15.52	17.11	18.85	20.85	23.70	27.42	30.80	Book Value per sh	43.80
146.40	146.40	146.29	146.44	146.43	146.83	154.78	154.71	154.58	154.67	154.71	155.93	158.40	162.78	167.08	174.78	177.98	180.00	Common Shs Outst'g (C)	185.00
17.4	11.3	14.5	15.1	11.8	11.7	11.4	9.1	7.0	8.7	5.1	6.0	5.3	6.8	5.9	6.4	8.6		Avg Ann'l P/E Ratio	11.0
.82	.72	.99	1.49	1.65	1.56	1.46	1.19	.95	.97	.88	.73	.58	.57	.55	.52	.58		Relative P/E Ratio	.90
3.9%	4.1%	3.0%	2.6%	3.0%	3.1%	3.2%	4.2%	4.9%	5.4%	6.3%	5.8%	6.1%	5.3%	5.9%	4.5%	3.1%		Avg Ann'l Div'd Yield	2.7%
28766	31664	38536	43488	51991	53522	58597	58023	64126	69375	76039	79000	Total Assets ($mill)	85000
13733	15895	18807	22158	25872	28220	31149	32974	35239	36278	33783	36000	Loans ($mill)	40000
516.8	521.0	563.0	636.7	778.2	750.8	986.7	1119.9	1051.8	1418.3	1557.3	1600	Net Interest Inc ($mill)	1850
88.2	47.6	33.6	29.8	42.1	51.2	114.0	230.0	150.0	335.0	265.0	180	Loan Loss Prov'n ($mill)	225
252.5	233.7	299.2	357.7	431.5	485.2	495.5	557.9	628.5	907.7	1281.0	1400	Noninterest Inc ($mill)	2250
324.9	347.1	409.3	470.0	573.4	612.0	703.3	797.1	856.1	1075.4	1407.3	1550	Noninterest Exp ($mill)	2150
262.8	218.3	286.9	288.3	387.7	374.5	441.7	480.0	520.3	705.4	872.5	825	Net Profit ($mill)	1200
40.1%	38.4%	38.5%	34.3%	38.1%	34.6%	34.8%	29.3%	22.8%	23.0%	25.2%	27.0%	Income Tax Rate	30.0%
.70%	.69%	.69%	.66%	.71%	.70%	.75%	.79%	.81%	1.02%	1.15%	1.15%	% Earned Total Assets	1.25%
545.9	622.5	523.3	580.1	577.2	526.0	709.0	793.0	786.0	1400.0	2334.0	2400	Long-Term Debt ($mill)	2400
1455.6	1591.8	1758.7	1949.3	2180.4	2420.0	2710.0	3319.0	3734.0	4362.0	5130.0	5700	Net Worth ($mill)	6100
5.1%	5.0%	4.8%	4.5%	4.2%	4.5%	4.6%	5.7%	5.8%	6.3%	6.8%	7.5%	% R W to Tot Assets	8.0%
47.7%	50.2%	48.8%	51.0%	50.0%	52.7%	53.2%	56.8%	55.0%	52.3%	44.4%	46.0%	% Loans to Tot Assets	54.0%
12.9%	13.7%	15.2%	14.8%	16.9%	15.5%	16.3%	13.9%	13.9%	16.1%	17.0%	16.0%	% Earned Net Worth	15.0%
9.1%	8.7%	10.2%	9.7%	11.8%	10.4%	11.3%	9.5%	9.6%	12.0%	13.0%	12.0%	% Retained to Comm Eq	10.0%
35%	38%	33%	35%	30%	33%	31%	37%	36%	30%	27%	29%	% All Div'ds to Net Prof	30%

CAPITAL STRUCTURE as of 12/31/86
LT Debt $2334.0 mill. **LT Interest** $220 mill
Due in 5 Yrs $500 mill.
Incl. $3 mill. capitalized leases.
Incl. $1 mill. 4¼% debs. ('87), callable 100, conv. into 38.28 shs. at $26.13; $16 mill. 4¾% debs. ('98), callable 102.14, conv into 25 shs. at $40.
Pension Liability None in '86 vs. None in '84
Pfd Stock $250.0 mill. **Pfd Div'd** $14.0 mill.
2,800,000 shs. Series A adjustable-rate (currently 5.625%) cum. pfd. redeemable at $100 from 3/1/86 to 2/9/88 and at $100 thereafter
Common Stock 177,959,045 shs.
(Adj. for stock split pd. 1/15/87.)

ASSETS (bank)	1984	1985	12/31/86
Loans	38239.0	36278.0	33783.0
Funds Sold	1989.0	2379.0	3988.0
Securities	9170.0	13675.0	17289.0
Other Earning	9729.0	9053.0	11062.0
Other	8019.0	8090.0	9937.0
LIABILITIES (bank)			
Deposits	38780.0	39845.0	42960.0
Funds Borrowed	16011.0	18614.0	20953.0
Long-Term Debt	786.0	1400.0	2334.0
Net Worth	3734.0	4362.0	5130.0
Other	4835.0	5124.0	4962.0
Total	84126.0	89378.0	76039.0
Loan Loss Reserv	683.0	793.0	910.0

ANNUAL RATES of change (per sh)	Past 10 Yrs	Past 5 Yrs	Est '84-'86 to '88-'90
Loans	8.5%	1.0%	5.0%
Earnings	9.5%	8.0%	10.0%
Dividends	7.5%	5.5%	10.0%
Book Value	9.0%	6.5%	12.5%
Total Assets	8.5%	5%	4.0%

Calendar	LOANS ($ mill.) Mar. 31	June 30	Sept. 30	Dec. 31
1983	32239	32325	31568	32974
1984	34112	35239	35176	35239
1985	34769	35228	36574	36278
1986	36489	37316	33471	33783
1987	34000	34000	35000	36000

Calendar	EARNINGS PER SHARE (A) Mar. 31	June 30	Sept. 30	Dec. 31	Full Year
1983	.69	.65	.58	.71	2.63
1984	.76	.55	.68	.95	2.94
1985	.93	.88	1.16	.94	3.91
1986	1.28	1.29	1.15	1.02	4.74
1987	1.25	1.25	1.30	1.30	5.10

Calendar	QUARTERLY DIVIDENDS PAID (B) Mar. 31	June 30	Sept. 30	Dec. 31	Full Year
1983	.231	.231	.231	.231	.93
1984	.25	.25	.25	.25	1.00
1985	.275	.275	.275	.275	1.10
1986	.306	.306	.306	.306	1.23
1987	.34				

BUSINESS: J.P. Morgan & Co., Inc. owns Morgan Guaranty Trust Company of New York (4th largest U.S. bank on basis of assets). Primarily serves large corporations. Has one of the largest trust departments in U.S. Branches in many foreign countries. Internat. earnings: 48% of consol. net profit. Net loan losses: 4% of average gross loans in '86. Loan loss reserve: 2.6% of gross loans outstanding at 12/31/86. Loan portfolio breakout at 12/31/85: domestic, 40%; foreign, 60%. Employee costs: 10% of gross income. Approx. 13,500 employees; 26,000 stockholders. Chairman: Lewis T. Preston. President: Dennis Weatherstone Inc.: Delaware. Address: 23 Wall Street, New York, New York 10015. Tel.: 212-483-2323.

J.P. Morgan's Timeliness rank has dropped a notch since our last report. Money center bank stocks have been generally weak performers in past months as investors have turned their attention away from interest rate-sensitive stocks. With interest rates now on a more even keel, after a striking two year decline, big earnings gains at most banks will be harder to come by. In addition, more problems have been brewing on the Latin American front. This year's debt negotiations with Brazil got off to a stormy start when that nation suspended interest payments on its medium and long term debt. If Brazil's moratorium on interest payments is extended, bank earnings could be penalized in 1987. (This bank had more than $1.8 billion in loans outstanding to Brazil at year-end 1985.) However, bank stocks are still selling at deep discounts to the market multiple, and J.P. Morgan still stands out from the herd as a company with favorable earnings growth prospects. We think 3- to 5-year share price appreciation potential is significant. Accordingly, patient investors may be interested in these shares.

Among the banks with big international exposures, Morgan's balance sheet is the best. At year-end 1986 Morgan's loan loss reserve stood at 2.62% of gross loans outstanding, the highest in the money center by a wide margin. The bank has about $840 million in accrued but unrealized investment securities gains on its books. And the bank's capital ratios are very high.

The balance sheet strength is extremely important. It means that recent earnings have been conservatively stated. It keeps the bank's cost of funds relatively low. And it provides a very good base for future earnings growth, since banks make money by leveraging their capital.

Morgan will probably keep expanding the range of its banking activities. Investment banking activities have become a more important source of profits for the bank as demand for commercial loans has waned. Already the bank has achieved prominent success in Eurobond underwriting, in private placements and in public finance. Recently, the bank has been beefing up merger and acquisitions advisory services.

Janet Lyons Richard T. Anderson

(A) Fully diluted earnings. In '70: 82¢ excl securities gains. '70: 8¢; '71: 15¢; '72: 4¢; '73: 3¢; '74: 18¢; '75: 10¢; '77: 2¢; '78: 12¢; '80: 32¢; '81: 33¢; '82: 57¢. Excl. nonrecurring gain: '84: 20¢. Next earnings report due late Apr. (B) Next dividend meeting about June 10. Goes ex about June 17. Dividend payment dates: Jan. 15, Apr. 15, July 15, Oct. 15. ■ Dividend reinvestment plan available (5% discount). (C) In mill., adjusted for stock splits & div'ds.

Company's Financial Strength	A++
Stock's Price Stability	95
Price Growth Persistence	50
Earnings Predictability	95

Factual material is obtained from sources believed to be reliable, but the publisher is not responsible for any errors or omissions contained herein.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

Case No. _____

In Re: KENDAVIS INDUSTRIES INTERNATIONAL, INC.; KENDAVIS HOLDING COMPANY, LOFFLAND BROTHERS COMPANY, MID CONTINENT SUPPLY COMPANY, GEODRIL, INC. LOFFLAND BROTHERS EASTERN HEMESPHERE, [sic] INC., and LOFFLAND BROTHERS (SINAPORE) [sic] PTE, LTD., *Debtors*	U.S. BANKRUPTCY COURT NORTHERN DISTRICT OF TEXAS CASE NO. 385-30348-A-11; (Administratively Consolidated) and UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION CASE NO. 3-86-2995-G

AFFIDAVIT OF JOHN THOMAS WARD IN SUPPORT OF EMERGENCY APPEAL TO THE U.S. COURT OF APPEALS FOR THE FIFTH CIRCUIT

STATE OF TEXAS
COUNTY OF TARRANT

BEFORE ME the undersigned authority on this 11th day of Arpil [sic], 1987, personally appeared John Thomas Ward, Assistant Manager, Internal Audit, for Kendavis Industries International, Inc., (hereinafter "Kendavis") who after being duly sworn by me did state upon his oath and of his own personal knowledge, as follows;

(1) My name is John Thomas Ward. I am above the age of 21 years old and fully qualified and competent to make this Affidavit.

(2) I have been employed by Kendavis Industries International, Inc. for twelve (12) years. I have been Assistant Manager of the Internal Audit Department of Kendavis for approximately six (6) years.

(3) I am personally familiar with the records of Kendavis which show the pre-petition creditors of Kendavis and its subsidiaries. The creditors which had claims against Kendavis and its subsidiaries at the time of the filing of the petitions for bankruptcy in the United States Bankruptcy Court for the Northern District of Texas are recorded by computer. Bankruptcy Case No. 385-30348-A-11 contains claims filed for such creditors.

(4) A personal inspection of the records of Kendavis and its subsidiaries shows that the following pre-petition creditors have claims against Kendavis and its subsidiaries:

	MIS CREDITOR NO.
FRIGETTE CORPORATION	
AT&T	0018509
HARRISBURG, INC.	
AT&T	0018501
AT&T	0018509
Amoco Oil Company ..... [formerly Standard Oil Co. (Indiana)]	0190501
Mississippi Power Co. ..... (Subsidiary of Mid-South Utilities)	2178500

	MIS CREDITOR NO.
LOFFLAND BROS.	
AT&T	0018500
AT&T	0018501
AT&T	0018502
AT&T	0018504
AT&T	0018506
AT&T	0018507
Amoco Oil Company	0190500
KENDAVIS INDUSTRIES INT'L., INC.	
AT&T	0018501
AT&T	0018504
Travelers	3208300
MIDCO EQUIPMENT CO.	
AT&T	0018501
AT&T	0018503
RIG-A-LITE COMPANY, INC.	
AT&T	0018501
MID-CONTINENT SUPPLY CO.	
AT&T	0018500
AT&T	0018501
AT&T	0018509
AT&T	0018510
Louisiana Power & Light (subsidiary of Mid-South Utilities)	1945503
Mississippi Power Co.	2178501
Mississippi Power & Light	2178000
SLIGO, INC.	
AT&T	0018501
Amoco Oil Company	0190502

	MIS CREDITOR NO.
UNIT RIG & EQUIPMENT CO.	
AT&T	0018500
AT&T	0018502
AT&T	0018505
AT&T	0018510
AT&T	0018511
AT&T	0018512
GLOBE MACHINERY AND SUPPLY COMPANY	
AT&T	0018501
AT&T	0018511
AT&T	0018512

(5) Globe Machinery and Supply Company, Unit Rig & Equipment Co., Sligo, Inc., Mid-Continent Supply Co., Rig-A-Lite, Midco Equipment Co., Kendavis Industries International, Inc., Loffland Brothers Company, Harrisburg, Inc. and Frigette Corporation are all subsidiaries of Kendavis Holding Company.

(6) I was requested to accumulate the information concerning the creditors listed in paragraph 4 on April 8, 1987. It was furnished to legal counsel for Kendavis and Mr. Ken Davis on April 11, 1987.

(7) Further affiant sayeth not.

SIGNED this 11th day of April, 1987.

/s/ JOHN T. WARD
John Thomas Ward
Assistant Manager Internal Audit,
Kendavis Industries International
Inc.

SUBSCRIBED AND SWORN to before me by John Thomas Ward this 11th day of April, 1987.

/s/ SUSAN CHESSHIRE
Notary Public in and for the
State of Texas

SUSAN CHESSHIRE, Notary Public
in and for the State of Texas
My Commission Expires 9-6-90.

Filed In The U.S. District Court, Northern District of Texas
on April 10, 1987

Entered On Docket Pursuant To F.R.C.P.
Rules 58 and 79a.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

In Re:

KENDAVIS HOLDING COMPANY, et al.,
Debtors

KENDAVIS HOLDING COMPANY, et al.,
Movants

vs.

OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, et al.,
Creditors/Respondents

C.A. No. 3-86-2995-G
(Hon. A. Joe Fish)

ORDER GRANTING COMMITTEES' MOTION TO QUASH NOTICE OF THE DAVIS FAMILY TO TAKE DEPOSITION OF THE HONORABLE ROBERT C. McGUIRE, UNITED STATES BANKRUPTCY JUDGE

CAME ON TO BE HEARD on this the *10* day of April, 1987 in said District, the Committees' Motion to Quash Notice of the Davis Family to Take Deposition of the Honorable Robert C. McGuire, United States Bankruptcy Judge, and Brief, and after consideration of the evidence before the court, the pleadings on file and argument of counsel, it appears to the court that said motion should be granted, it is therefore:

ORDERED that the Committees' Motion to Quash Motion of the Davis Family to Take Deposition of the Honorable Robert C. McGuire, United States Bankruptcy Judge shall be in all things granted; it is further

ORDERED that the deposition of the Honorable Robert C. McGuire, United States Bankruptcy Judge, which is scheduled to commence at 10:00 o'clock a.m. on April 11, 1987 and continuing thereafter from day to day until completed shall be quashed by order of this court.

SIGNED this the *10* day of April, 1987 in Dallas, Texas.

/s/ A. JOE FISH
United States District Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

In Re:

KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY and LOFFLAND BROTHERS COMPANY,
Debtors

Case No. 385-30348-M-11 (Administratively Consolidated)

ORDER SUSPENDING THE TAKING OF THE DEPOSITION OF THE HONORABLE ROBERT C. McGUIRE, UNITED STATES BANKRUPTCY JUDGE

CAME ON FOR HEARING on this _____ day of April, 1987, in said District, the Committee's Motion to Quash Notice Of The Davis Family to Take Deposition Of The Honorable Robert C. McGuire, United States Bankruptcy Judge and Brief, and the Davises' Objection to the Committees' Motion to Quash Notice Of The Davis Family To Take Deposition of the Honorable Robert C. McGuire, United States Bankruptcy Judge, and Brief, and after consideration of the pleadings on file and arguments of counsel, it appears to the Court that the deposition of the Honorable Robert C. McGuire should be suspended pending further order from either the United States District Court for the Northern District of Texas or the Fifth Circuit Court of Appeals; it is therefore

ORDERED that the deposition of the Honorable Robert C. McGuire rescheduled for April 18, 1987, at 10:00 o'clock a.m. is indefinitely suspended pending further order from either the United States District Court for the Northern District of Texas or the Fifth Circuit Court of Appeals.

SIGNED this _____ day of April, 1987.

_____
United States Bankruptcy Judge

APPROVED AS TO FORM ONLY:

Shannon, Gracey, Ratliff &
Miller
2200 First City Bank Tower
Fort Worth, Texas 76102

By: /s/ S. A. GOODWIN
Stephen A. Goodwin
Attorneys For The Committees

Brown, Herman, Scott
Dean & Miles
203 Fort Worth Club Building
Fort Worth, Texas 76102

By: /s/ JOHN G. TRUELSON
John G. Truelson

Attorneys For The Davis Family

Supreme Court, U.S.
FILED
DEC 21 1987
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A.T. DAVIS, A.T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A.T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T.C. DAVIS, II, T.C. DAVIS, II TRUST, T.C. DAVIS, II TRUST "A", T.C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T.C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF RESPONDENT THE BANK OF NOVA SCOTIA IN OPPOSITION

GEORGE J. WADE
Counsel of Record

SHEARMAN & STERLING
153 East 53rd Street
New York, New York 10022
(212) 848-4000

Attorneys for Respondent The Bank of Nova Scotia

Rule 28.1 Listing of Parents, Subsidiaries and Affiliates of The Bank of Nova Scotia

The Bank of Nova Scotia Jamaica Limited
The Bank of Nova Scotia Trust Company Jamaica Limited
The Bank of Nova Scotia Trust Company of New York
The Bank of Nova Scotia Trinidad & Tobago Limited
The Bank of Nova Scotia Trust Company of Trinidad and Tobago Limited
Banc-Merc Investment Group Inc.
Brunswick Square Limited
Canborough Limited
The Canborough Corporation
Caribbean Credit Corporation N.V.
Caribbean Credit Corporation (Curacao) N.V.
Caribbean Mercantile Bank N.V.
Chargex Limited
Export Finance Corporation of Canada Limited
Fredericton Developments Limited
Kings Place Parking Limited
ICIC Holdings Limited
Industrial Credit Insurance Company
Maduro & Curiel's Bank N.V.
Maduro & Curiel's Bank (Bonaire) N.V.
Maduro & Curiel's Insurance Services N.V.
N.V. De Curacaosche Hypotheekbank
N.V. De Spaar En Beleenbank Van Curacao
N.V. Trust—En Administratie Maatschappij Van Maduro & Curiel's Bank N.V.
Progress N.V.
Scotia Centre Limited
Scotia Mortgage Corporation
Scotia-Toronto Dominion Leasing Limited
Scotiabank de Puerto Rico
The West India Company of Merchant Bankers Limited
The Windward Islands Bank Limited

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A.T. DAVIS, A.T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A.T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T.C. DAVIS, II, T.C. DAVIS, II TRUST, T.C. DAVIS, II TRUST "A", T.C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T.C. DAVIS,

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v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF RESPONDENT THE BANK OF NOVA SCOTIA IN OPPOSITION

STATEMENT OF THE CASE AND SUMMARY OF ARGUMENT

These cases were commenced by the filing of involuntary petitions for reorganization in the United States Bankruptcy Court for the Northern District of Texas on February 21, 1985, and orders for relief were entered by consent on March 11 and 13, 1985. It was not

until November 24, 1986 that the Creditors' Committees' Plan of Reorganization was confirmed by order of Bankruptcy Judge McGuire, affirmed by District Judge Fish on March 26, 1987 and consummated on April 16, 1987.

The Bank of Nova Scotia is the largest creditor of the debtors, being owed $67,235,555.78 in principal amount. One of the major bank creditors and an active participant in the reorganization case was Morgan Guaranty Trust Company of New York ("Morgan Guaranty"). Petitioners are the former stockholders of the admittedly insolvent debtors.

After having shepherded this case through more than a year and a half of intense negotiations and litigation, on March 23, 1987, Bankruptcy Judge McGuire informed counsel that he had the night before learned that Morgan Guaranty was a wholly owned subsidiary of J.P. Morgan & Co. Incorporated ("J.P. Morgan"), in which he held approximately $36,000 of common stock as trustee for himself and his family. He immediately recused himself from further proceedings in the cases, which were assigned to Bankruptcy Judge Harold C. Abramson. Judge McGuire stated on the record, and there is no reason to doubt, that he did not know of the existence of the conflict raised by J.P. Morgan's ownership of Morgan Guaranty until the time that he informed counsel.

Petitioners do not quarrel with any of the above nor with Judge McGuire's immediate recusal; instead they seek to void orders of confirmation of plans of reorganization in these cases. To accomplish what? To vindicate a statute in which "knows" is the operative word? To punish a Bankruptcy Judge who acted immediately upon learning the facts? Or is it just to reargue on remand points that the Court of Appeals for the Fifth Circuit held to be "frivolous"? Indeed, since the debtor corporations are admittedly insolvent, rendering their stock worthless, these Petitioners lack standing on remand and in fact now do not have any financial stake in the outcome of these cases.

As the party with the largest stake in these proceedings, The Bank of Nova Scotia urges this Court to deny certiorari and finally to put an end to this litigation.

ARGUMENT

I

JUDGE McGUIRE FULLY COMPLIED WITH SECTION 455

Immediately upon learning of his financial interest in the parent of Morgan Guaranty, Judge McGuire recused himself. Thus, he fully complied with both Sections 455(a) and 455(b)(4).

Petitioners try two stratagems to get around that fact. The first is to argue that, despite the fact that Judge McGuire did not know of his indirect financial interest in a creditor before March 23, 1987, an objective observer could think that he did creating an appearance of impropriety. That argument is flawed because it would read the knowledge requirement out of Section 455(b)(4). There is nothing in the legislative history to suggest that Congress placed the phrase "he knows" in the statute merely to have it ignored. Section 455 is structured so that (i) a judge must disqualify himself when there is a reasonable question as to his impartiality and (ii) "[h]e shall *also* disqualify himself . . . [when] [h]e *knows* that he . . . has a financial interest." [Emphasis added.] The language of the statute indicates that financial interest is a separate ground for disqualification covered only by subsection (b)(4).

While, as Petitioners claim, "the theme [of the legislative history] is the promotion and protection of public and litigant confidence in the impartiality of judicial decisions," Petitioners' Brief at 9, it does not promote or protect anyone's interest to void decisions rendered by judges who did not even know they had a basis for a bias. No court has done this. There is no need for this Court to take this case and impose such a rule for the first time.

Moreover, even the "constructive knowledge" or "objective observer" standard of the Fifth Circuit, which is already before this Court in *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986), *cert. granted*, 107 S. Ct. 1368 (1987), was satisfied in this case. Judge McGuire on taking this case inquired of his stockbroker, who he thought was an authoritative source as to whether there was any connection between Morgan Stanley and J.P. Morgan. After a busy judge received an assurance that there was no such connection, it cannot be said that an objective person would expect him to inquire further. Thus, the District Court specifically found that an objective observer would not quarrel with Judge McGuire's behavior. P. Appendix at 15-16. The Fifth Circuit has correctly emphasized that "[w]here a reasonable person would only speculate that a judge might have actual knowledge of the

facts, constructive knowledge does not exist." *Health Services*, 796 F.2d at 803.

Finally, for Petitioners to claim that Judge McGuire's statements were "unsworn" is ludicrous and offensive. If Judge McGuire would misstate the facts before parties to a case and a court reporter, clearly "swearing" would be pointless.

Petitioners' second stratagem to avoid the fact that Judge McGuire complied with Section 455 is to ask this Court to impose a rule that any mistake or lack of full information, regardless of its impact on a judge's decisions or the litigants before him, should be "remedied" by sending all the litigants back to the inception of the case. No court has done this, and it is unnecessary for this Court to consider doing so now.

Section 455(c) provides in relevant part that "[a] judge should inform himself about his personal and fiduciary financial interests." 28 U.S.C. § 455(c). It does not make him an insurer that the information he receives upon an inquiry is infallible. It does not require that, in the event of an error in the judge's information that does not result in actual bias, an enormous burden should be placed on one litigant to the sole benefit of the other.

II

THERE IS NO JUSTIFICATION FOR THE DRASTIC REMEDY THAT PETITIONERS SEEK TO IMPOSE

Petitioners ask the rhetorical question, "[h]ow can the public and losing litigants be satisfied by being told the judge failed to know what he owned?" Petitioners' Brief at 17. The Bank of Nova Scotia submits that the District Court was correct in concluding that the "public," in the guise of the "reasonable person" or "objective observer," would not be shocked or distressed that Judge McGuire was not aware of all the details of what he owned. In fact, The Bank of Nova Scotia submits that the public would lose faith in a judicial process that forced winning litigants to repeat two years of litigation because of an abstract concern with appearances when there is no actual bias. And losing litigants (and especially those whose substantive claims are "frivolous") do not need protection from a judge who has no bias because he lacks any knowledge of why he could, arguably, be biased.

As for the losing litigants in this case, their claims, which they ask this Court to give them the opportunity to relitigate, were described

by the Fifth Circuit as "frivolous." Thus, reversal and remand can only operate to return these cases for relitigation of frivolous contentions. Petitioners indeed have no cause to complain and no stake in the outcome; they are the former shareholders of admittedly insolvent companies that owed Respondent The Bank of Nova Scotia alone over $67,000,000.

Moreover, under the rule and remedy Petitioners ask this Court to impose, winning litigants would have no way to protect themselves from a reversal of all their efforts after two, five or any number of years had passed. In this case, Petitioners could have checked the public disclosure list of Judge McGuire's stock ownership on file in the Bankruptcy Court and, had they known the connection between J.P. Morgan and Morgan Guaranty, moved for recusal. Petitioners did not do so, and they should not be permitted a "free shot" at relitigating their position. Further, in other circumstances, where a judge honestly but mistakenly believed that he did not own stock in a party and hence the ownership did not appear on court records, there would be no way for a winning litigant to protect itself from a later voiding of the judgment it had obtained. Thus, the winning litigant would be prejudiced and yet have been unable to protect itself, and the losing litigant would have the benefit of another attempt to litigate even when it was not actually prejudiced.

CONCLUSION

This Court should not grant certiorari in this case. There is no outstanding cause to be vindicated and no conflict among Circuits to be resolved. There is only the petition of those whose substantive claims are "frivolous," who lack a financial stake in the outcome, and who would further delay the rightful reorganization of corporations with over $500 million of debt.

Respectfully submitted.

/s/ GEORGE J. WADE

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Supreme Court, U.S.
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CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY and KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K. W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A," A. T. DAVIS, A. T. DAVIS TRUST "A," KAY DAVIS, KAY DAVIS TRUST "A," TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A. T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T. C. DAVIS, II, T. C. DAVIS, II TRUST, T. C. DAVIS, II TRUST "A," T. C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A," BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T. C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC. AND LOFFLAND BROTHERS COMPANY, KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

RESPONDENT KENDAVIS HOLDING COMPANY'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether a judge is disqualified under 28 U.S.C. § 455(b)(4) despite his lack of knowledge that he owns a financial interest in the corporate parent of a party to the proceeding.

2. Whether 28 U.S.C. § 455(c) creates a conclusive presumption that a judge knows everything about his or her financial and fiduciary interests that is revealed in materials in the judge's possession.

3. Whether the general rule that judges who learn of a disqualifying interest are required only to recuse themselves from future proceedings should be abandoned in favor of a rule that all orders entered by a disqualified judge are void, even in the absence of any showing of actual bias or impartiality.

4. Whether an appeal of the denial of motions to vacate the entered orders of a bankruptcy judge who later recused himself is rendered moot by the substantially complete implementation of those prior orders.

PARTIES TO THE PROCEEDING BELOW

In addition to the parties named in the caption of this case, the following were made parties to the proceeding in the Fifth Circuit:

The Bank of New York
The Chase Manhattan Bank, N.A.
Credit Commercial De France, New York Branch
Cummins Sales & Service, Inc.
Den Norske Creditbank
Development Bank of Singapore Limited
First City National Bank of Fort Worth
First City National Bank of Houston
First Interstate Bank of California
First National Bank & Trust Company of Oklahoma City (now known as Consolidated Asset Management as Administrator for Federal Deposit Insurance Corporation, in its corporate capacity)
First National Bank of Fort Worth
First RepublicBank Dallas, N.A.
First RepublicBank Fort Worth, N.A.
Frigette Corporation
Geodril, Inc.
Globe Machinery and Supply Company
Harrisburg, Inc.
InterFirst Bank Fort Worth, N.A.
Irving Trust Company
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers Eastern Hemisphere, Inc.
Loffland Brothers (Singapore) Pte., Ltd.
Mechanical Rubber Products Corporation
Miami-Dickerson Steel Company
Midco Equipment Co.
Mid-Continent Supply Co.
Moore & Sons, Inc.
Morgan Guaranty Trust Company of New York
The National Commercial Bank of Saudi Arabia
Nippon Kokan Kabushiki Kaisha
Rig-A-Lite Company, Inc.
Security Pacific National Bank
Sligo, Inc.
State Pipe & Supply Co.
Texas American Bank (Fort Worth), N.A.
Unit Rig & Equipment Co.

All of these companies are either banks that were members of the Official Unsecured Creditors' Committees or corporate affiliates of Kendavis Holding Company. Kendavis Holding Company has no corporate parent. Its affiliates, other than wholly-owned subsidiaries and the affiliates listed above, are:

CS&S Liquidating Co.
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers (Malaysia) Sdn. Bhd.
Mid-Continent Supply Co.
Nadrico Saudi Limited
State Pipe and Supply Co.
Stratoflex, Inc.
Unit Rig & Equipment Co.
Loffland Brothers de Venezuela, C.A.
Cumvenca, C.A.
Cummins Sales & Service de Venezuela, C.A.
KECO Limited

Upon the request of its clerk, the United States Court of Appeals for the Fifth Circuit was provided with a list of all pre-petition creditors in the various Kendavis cases. The list identified approximately 10,835 individuals and entities. If this Court so desires, copies of this list can be prepared and forwarded to the Court.

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No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY and KENDAVIS INDUSTRIES INTERNATIONAL, INC.

Debtors

K. W. DAVIS, JR., et al.,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES, et al.,

Respondents

RESPONDENT KENDAVIS HOLDING COMPANY'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The *per curiam* opinion of the United States Court of Appeals for the Fifth Circuit is unreported and is reprinted in the appendix to the petition at p. 6 ("Pet. App. 6"). The Memorandum Order of the United States District Court for Northern District of Texas, Dallas Division, is unpublished and is reprinted at Pet. App. 11.

JURISDICTION

Petitioners have applied for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit. There is no jurisdiction in this case because petitioners lack standing to assert their claims, and the unavailability of any effective relief renders petitioners' claims moot thereby negating the existence of a case or controversy justiciable under Article III of the Constitution. *See* U.S. Const., Art. III, § 2, cl. 1.

RELEVANT CONSTITUTIONAL AND STATUTORY PROVISIONS

United States Const., Article III, Section 2, Clause 1:

The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority, — to all Cases affecting Ambassadors, other public Ministers and Consuls; — to all Cases of admiralty and maritime Jurisdiction; — to Controversies to which the United States shall be a Party; — to Controversies between two or more States; — between a State and Citizens of another State; — between citizens of different States, — between citizens of the same State claiming Lands under Grants of different States, and between a State, or the Citizens thereof, and foreign States, Citizens or Subjects.

United States Const., Amend. V:

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

28 U.S.C. § 455 (1982):

(a) Any justice, judge, or magistrate of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

(b) He shall also disqualify himself in the following circumstances:

(1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

(2) Where in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it;

(3) Where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy;

(4) He knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding;

(5) He or his spouse, or a person within the third degree of relationship to either of them, or the spouse of such a person:

(i) Is a party to the proceeding, or an officer, director, or trustee of a party;

(ii) Is acting as a lawyer in the proceeding;

(iii) Is known by the judge to have an interest that could be substantially affected by the outcome of the proceeding;

(iv) Is to the judge's knowledge likely to be a material witness in the proceeding.

(c) A judge should inform himself about his personal and fiduciary financial interests, and make a reasonable effort to inform himself about the personal financial interests of his spouse and minor children residing in his household.

(d) For the purposes of this section the following words or phrases shall have the meaning indicated:

(1) "proceeding" includes pretrial, trial, appellate review, or other stages of litigation;

(2) the degree of relationship is calculated according to the civil law system;

(3) "fiduciary" includes such relationships as executor, administrator, trustee, and guardian;

(4) "financial interest" means ownership of a legal or equitable interest, however small, or a relationship as a director, adviser, or other active participant in the affairs of a party, except that:

(i) Ownership in a mutual or common investment fund that holds securities is not a "financial interest" in such securities unless the judge participates in the management of the fund;

(ii) An office in an educational, religious, charitable, fraternal, or civic organization is not a "financial interest" in securities held by the organization;

(iii) The proprietary interest of a policyholder in a mutual insurance company, of a depositor in a mutual savings association, or a similar proprietary interest, is a "financial interest" in the organization only if the outcome of the proceeding could substantially affect the value of the interest;

(iv) Ownership of government securities is a "financial interest" in the issuer only if the outcome of the proceeding could substantially affect the value of the securities.

(e) No justice, judge, or magistrate shall accept from the parties to the proceeding a waiver of any ground for disqualification enumerated in subsection (b). Where the ground for disqualification arises only under subsection (a), waiver may be accepted provided it is preceded by a full disclosure on the record of the basis for disqualification.

STATEMENT OF THE CASE

Petitioners are either members of the family of the late Kenneth W. Davis, Sr. or are trusts, foundations or estates affiliated with the Davis family. Prior to April 16, 1987, Petitioners ("the Davis Family") held all outstanding shares of stock of respondent Kendavis Holding Company ("KHC"), which in turn owned all of the outstanding stock of Kendavis Industries International, Inc. ("KIII").

Certain creditors of KHC and KIII filed involuntary petitions for relief under chapter 11 of title 11 of the United States Code ("the Bankruptcy Code") against KHC and KIII on February 21, 1985. KHC and KIII consented to the entry of orders for relief, which United States Bankruptcy Judge Robert C. McGuire entered on March 19, 1985.

On November 24, 1986, after over 20 months of proceedings during which hundreds of orders were entered, Judge McGuire entered an order confirming a plan of reorganization for KHC and KIII ("the Confirmation Order"). Among other things, the confirmed plan provided that upon its effective date, KIII would be merged into KHC, the previously outstanding shares of stock of KHC would be cancelled, and new shares would be issued to holders of allowed Class 7 claims.

On the same day Judge McGuire entered the Confirmation Order, respondent KHC and certain of its subsidiaries, which were then under the control of the Davis Family,[1] filed an appeal of the Confirmation Order with the United States District Court for the Northern District of Texas, Dallas Division. The Davis Family appealed the Confirmation Order on December 4, 1986.

The District Court, in a series of orders entered on March 26, 1987, dismissed the appeals of the Confirmation Order filed by the Davis Family and the KHC entities, ruling that KHC and KIII's insolvency denied standing to KHC, KIII and the

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[1] Petitioner K. W. Davis, Jr. was then Chairman of the Board and President of KHC; T. Cullen Davis was Vice President of KHC; and petitioner Kay Davis was Secretary of KHC.

Davis Family as shareholders.[2] The District Court also denied the appellants' motions for a stay of implementation of the confirmed plan. R. App. 9, 11. The KHC entities and the Davis Family appealed to the United States Court of Appeals for the Fifth Circuit. On April 9 and April 10, the KHC entities filed motions seeking an expedited appeal of the Confirmation Order and a stay of implementation of the confirmed plan pending appeal.

On March 23, 1987, Bankruptcy Judge McGuire held a telephone conference with former counsel for respondent KHC and counsel for the Official Unsecured Creditors' Committees for KHC and KIII, during which Judge McGuire informed counsel that he had discovered the previous evening that a company in which he owned stock (J.P. Morgan Company, Inc.) was the owner of Morgan Guaranty Trust Company of New York, one of the bank creditors of KHC and KIII. See Pet. App. 18-21. Judge McGuire advised counsel that he had previously investigated the possible relationship of the two companies by making inquiry to his broker, and had been told they were unrelated. Judge McGuire explained that he had learned of the relationship when reviewing *The Value Line Investment Survey*, a quarterly investment report. Although Judge McGuire scheduled a status conference for March 26, 1987 to address procedures by which the disqualification issues might be resolved, the status conference was never held. Judge McGuire instead voluntarily recused himself on March 26, 1987.

On March 31, 1987, based on Judge McGuire's recusal, the Davis Family and the KHC entities filed motions with the District Court to vacate certain of Judge McGuire's orders, including the Confirmation Order. The District Court denied the motions to vacate on April 10, 1987 on the basis that Judge

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[2] The District Court's orders are reprinted in the Joint Appendix to Briefs in Opposition of Respondents Kendavis Holding Company and the Official Unsecured Creditors' Committees at pp. 1-11 ("R. App. 1-11").

McGuire's previous rulings should stand because he was not disqualified under either Section 455(a) or (b) until he discovered the relationship between J. P. Morgan & Sons and Morgan Guaranty. Pet. App. 11-17.

Upon the District Court's denial of the motions to vacate, the Davis Family and the KHC entities filed additional motions with the Fifth Circuit seeking an emergency stay of the effective date of the confirmed plan. The Fifth Circuit denied all motions for a stay by order of April 15, 1987; the Fifth Circuit, however, granted the motions for an expedited appeal.

As a result of the denials of any stay, the confirmed plan became effective on April 16, 1987. The Davis Family's stock was cancelled, KIII was merged into KHC, and KHC came under the control of new management. Since April 16, KHC has implemented the confirmed plan. Among other events, involuntary petitions for relief pending against twelve of KHC's subsidiaries were dismissed.[3]

Also, the KHC entities that, under former management, had appealed the Confirmation Order, retained new counsel and sought to dismiss the appeals pending before the Fifth Circuit as not in the best interests of the companies. KHC's former counsel, however, sought to continue to prosecute the appeal without authority from KHC. The Fifth Circuit permitted KHC's former counsel to participate in the appeal and to argue on behalf of KHC's former management.[4] The Fifth Circuit rendered the decision that is the subject of the Davis Family's petition on September 24, 1987.

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[3] Some of the more important actions taken to implement the confirmed plan are set forth in the Amended Affidavit of David E. Hawthorne, which was filed with the Fifth Circuit and which is reprinted at R. App. 12-24.

[4] The reference in the Fifth Circuit's opinion that "former management . . . claim[ed] rights of representation of creditors that can now be fully paid" refers to the argument of KHC's former counsel that, by virtue of their prior representation of KHC and KIII as debtors in possession, the Bankruptcy Code made them trustees for KHC and KIII's creditors.

SUMMARY OF THE ARGUMENT

Certiorari is unwarranted because the Fifth Circuit and the District Court properly applied 28 U.S.C. § 455(a) and (b) in holding that, under the circumstances, Bankruptcy Judge McGuire was not disqualified until he knew that he held a financial interest in the corporate parent of a party. The Davis Family attempts to avoid the assessment of particular facts properly made by the courts below by arguing that 28 U.S.C. § 455(c) creates a conclusive presumption of knowledge. Such a rule has never been accepted by any court, is unsupported by the statute and the legislative history, and would do violence to Congress' intent to fashion a practical solution to the practical problems of judicial disqualifications.

In addition, dismissal of the petition is appropriate. The implementation of the confirmed plan has rendered the Davis Family's appeal moot, and the Davis Family, as the former shareholders of an admittedly insolvent corporation, lack standing to assert their claims.

REASONS THE WRIT SHOULD NOT BE GRANTED

The Davis Family seeks this Court's review of a decision that the Fifth Circuit decided to render *per curiam* and unpublished because it had no precedential value and merely decided a particular case on the basis of well-settled principles of law. Pet. App. 6. Indeed, insofar as 28 U.S.C. § 455 is concerned, the Fifth Circuit opinion simply affirmed two factual findings by the District Court: one, a finding that Judge McGuire did not have actual knowledge of a financial interest; and two, a finding that a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual knowledge of his financial interest. Pet. App. 7, 14-15. As a result of the first finding, the district court concluded that Section 455(b) had not been violated. As a result of both findings, the district court concluded that Section 455(a) was not violated.

Stripped of its rhetoric, the Davis Family's petition is nothing more than an attempt to overturn the District Court's second finding by construing Section 455(b) in such a way as to eliminate the word "know" from the statute.[5] Interestingly, the Davis Family's argument begins with the admission that the District Court's first finding is correct — the judge did not have actual knowledge of an interest. "The bankruptcy judge . . . failed to recognize that substantially the entire business of J.P. Morgan was the ownership of Morgan Guaranty." Petition, p. 5. The Davis Family then argues that since the judge possessed information revealing the relationship, he should have known of the relationship, and since he should have known, "he must be concluded to have known . . .." Petition, p. 5.

The Davis Family can blind themselves to reality in this way only by resort to the procedural device of a conclusive presumption. Thus, the Davis Family urges that Section 455(b)(4) and Section 455(c), read together, "establish a standard by which a judge is charged, *conclusively*, with knowledge of that which information in his possession reveals about his financial interest . . .." Petition p. 15 (emphasis supplied). No court has accepted this proposition. One district court has expressly rejected it. *NEC Corp. v. Intel Corp.*, 654 F. Supp. 1256, 1257-58 (N.D. Cal.), *appeal docketed*, No. 87-7126 (9th Cir.) (March 30, 1987). Two circuit courts, in addition to the Fifth Circuit, have implicitly rejected the

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[5] Although the petition does not identify Section 455(a) in the Questions Presented, the Davis Family does suggest that the Fifth Circuit abandoned its construction of Section 455(a) in *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796 (5th Cir. 1986), *cert. granted*, ___ U.S. ___, 107 S. Ct. 1368 (1987) (No. 86-957) (argued December 9, 1987). Petition, pp. 6-7. This suggestion is curious in light of the District Court's express conclusion that "a reasonable person, knowing all the surrounding circumstances, would not expect that Judge McGuire had actual or constructive knowledge of any conflict," Pet. App. 15-16, and the Fifth Circuit's conclusion that "we think it clear that the bankruptcy judge's impartiality could not be reasonably questioned." Pet. App. 7. No departure from the *Health Services* test is apparent — only a different conclusion based on different facts.

proposition. *See Davis v. Xerox*, 811 F.2d 1293, 1296 (9th Cir. 1986), *cert. denied*, ___ U.S. ___, 56 U.S.L.W. 3383 (Nov. 30, 1987) ("We are unwilling to presume that because the judge once knew, he could not have forgotten"); *Hodosh v. Block Drug Co.*, 790 F.2d 880 (Fed. Cir.), *cert. denied*, ___ U.S. ___, 107 S. Ct. 106 (1986) (no basis for disqualification where judge did not know that a company in which his spouse owned stock acquired a party to the proceeding); *Union Carbide Corp. v. U.S. Cutting Service, Inc.*, 782 F.2d 710, 713-15 (7th Cir. 1986) (judge permitted to continue to sit in class action case when, after discovering that two companies in which her spouse held stock were unnamed class members, she had her spouse dispose of the stock).

Yet the existence of a conclusive presumption of knowledge is central to the Davis Family's petition; without it, they are left with the facts that even they admit — Judge McGuire did not know of the relationship between J. P. Morgan and Morgan Guaranty, Petition, p. 5, and his "actual, subjective integrity is not called into question." Petition, p. 18. Recognizing the importance to their position of a conclusive presumption, the Davis Family argues that "[a]ny other position vitiates § 455(b)(4)." *Id.* To the contrary, adoption of a conclusive presumption is precisely what Congress sought to avoid when it rejected a version of the financial interest subsection of Section 455 that did not include a knowledge test in favor of the present statute, which does include a knowledge test.

In Enacting 28 U.S.C. § 455, Congress Sought a Practical Solution to Practical Problems

Unable to cite any judicial precedent for their proposition, the Davis Family selectively refers to the legislative history of Section 455 to suggest that the overwhelming concern of Congress in enacting Section 455 was to foster public confidence by avoiding the appearance of impropriety. Aside from the fact that public confidence in the judiciary and the appear-

ance of propriety are both promoted by Judge McGuire's courage in coming forward and voluntarily recusing himself as soon as he learned of his financial interest, the Davis Family has ignored an equal, if not greater concern of Congress — the dilemma faced by every judge who had tried to find guidance for his conduct in the vague statute that preceded the current one. The former version of Section 455 provided:

> Any justice or judge of the United States shall disqualify himself in any case in which he has a substantial interest, has been of counsel, is or has been a material witness, or is so related to or connected with any party or his attorney as to render it improper, in his opinion, for him to sit on the trial, appeal or other proceeding therein.

Act of June 25, 1948, c. 646, § 1, 62 Stat. 908 (1948) (current version at 28 U.S.C. § 455 (1982)).

The Congressional hearings and reports make repeated reference to Congress' desire to replace the uncertain test of the former statute with a clear and certain standard for judges. *E.g.*, H. Rep. No. 93-1453, 93d Cong. 2d Sess. (1974), reprinted in 1974 U.S. Code Cong. and Admin. News 6351 ("House Report") at 6352, 6355; *Judicial Disqualification: Hearing on S. 1064 Before the Subcommittee on Improvements in Judicial Machinery of the Committee on the Judiciary, United States Senate*, 93d Cong. 1st Sess. 24 (1973) ("Senate Hearings") (hearings were held in the Senate on both July 14, 1971 and May 17, 1973, and were reported in the single volume cited above). For example, Senator Burdick opened both the 1971 and 1973 Senate hearings by noting that the legal standard created by the then-existing statute had the effect of "placing a judge on the horns of a dilemma." Senate Hearings at 2, 74.[6] The uncertainty of the rule that a judge was disqualified only

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[6] The current version of Section 455 is the result of Congressional hearings in 1971 and 1973, during which Congress considered three different bills on judicial disqualification. S. 1553 was introduced by Senator Hollings, and S. 1886 was introduced by Senator Bayh, both in 1971. In 1973, the bill before the Senate, S. 1064, was introduced by Senator Burdick and was based on the newly adopted ABA Code of Judicial Conduct.

for a "substantial interest," coupled with the existing case law that the judge had a "duty to sit" unless disqualified, *e.g.*, *Edwards v. United States*, 334 F.2d 360, 362 n.2 (5th Cir. 1964), *cert. denied*, 379 U.S. 1000 (1965), left many judges to act at their own peril.

Indeed, as the Davis Family notes, Petition, pp. 8-9, the new legislation was inspired in part by the controversy surrounding the nomination of Judge Haynsworth to this Court. Senator Hollings first tried to amend the disqualification statute during the Haynsworth hearings, when he saw the inequitable position into which Judge Haynsworth had been forced by the vague "substantial interest" and "in his opinion" standards. Senate Hearings at 24. Although the American Bar Association cleared Judge Haynsworth of any misconduct for failing to disqualify himself in certain cases on the basis of financial interest, many considered the resulting "cloud of doubt" to be unfair to the judge. Senate Hearings at 24. Section 455 was designed to eliminate the uncertainty. As Senator Burdick noted at the 1973 hearings:

> It is believed that the enactment of this bill will do much to remove our Federal judges from the horns of the dilemma they currently face. Congress will have specified the amount and type of financial interest, the degree of relationship, and the prior association which forces disqualification. Congress will have relieved the Judge of the "duty-to-sit" which presently clouds his judgment when he is forced to determine whether his interest is a case so "substantial" as to require his disqualification.

Senate Hearings at 74.

Given Congress' concern that judges needed a clear, workable standard for determining when they were disqualified, the legislative history reflects that the concept of Section 455 was to promote the appearance of impartiality not by imposing draconian punishments for failing to abide by impossible standards, but by establishing standards that judges

could readily implement. In the 1971 Senate hearings, Professor John P. Frank stated that "[t]he goal is to get to something which is practical enough to be livable." Senate Hearings at 37. Senator Hollings described his bill as "a comprehensive but practical approach to judicial disqualification." Senate Hearings at 24. The final statute explicitly deals with the Congressional concern over one particular practical problem — the impossibility of keeping track of the holdings of a mutual fund — by exempting mutual funds from the general rule. 28 U.S.C. § 455(d)(4)(i) (1982). Similarly, the knowledge requirement of Section 455(b)(4) stems from Congressional recognition that a workable standard must be consistent with the practical problems of everyday compliance.

The knowledge requirement of Section 455(b)(4) was deliberately added in light of express recognition by the Senate of the practical problems that would result if knowledge were not required. Senator Bayh's bill differed from the other bills and the statute ultimately adopted in that it required a judge to disqualify himself "in any case in which he has an interest," rather than when he *knows* that he has a financial interest. *Compare* S. 1886, Senate Hearings at 6 (the Bayh bill) *with* S. 1553, Senate Hearings at 3 (the Hollings bill) *and* S. 1064, Senate Hearings at 130 (the Burdick bill). *See also* 28 U.S.C. § 455(b)(4) (1982).

The practical problems with the Bayh bill came to light during the Senator's testimony:

> Senator GURNEY: . . . I think it might be difficult, perhaps, sometimes for a judge to keep track, possibly, of the holdings of a major corporation in subsidiaries, and he might have known them at the time he acquired his stock but there might be changes made later on. Suppose he ran afoul of this particular provision in your bill unwittingly and unknowingly, what happens if he goes ahead and tries the case?
>
> Senator BAYH: Well, I think that case would then be subject to reversal on appeal.

> Senator GURNEY: Well, suppose it were not discovered until the case was through; then what?
>
> Senator BAYH: Then, it would have to be considered on its merits at the time. You have to consider each case on its merits.
>
> * * *
>
> Senator GURNEY: My question is directed as to what is going to happen to the litigation in cases and the respective rights of the parties if the case is tried and unwittingly falls within this rule?
>
> If we are going to pass a bill here, *we had better make darn sure that we have got a bill that is not going to cause all kinds of problems down the road.*

Senate Hearings, at 17, 18 (emphasis supplied). Senators Burdick and Gurney then commented on the practical benefits of the knowledge requirement in the ABA Code of Judicial Conduct:

> Senator BURDICK: I wonder if the answer might lie in the ABA's suggestion that they base this interest in subsidiaries on knowledge, the judge, if he knew? If he knows that he individually, or his fiduciary, or other member of his immediate family, or any member of his family residing in the household has a financial interest, if he knows of the interest, it is based upon knowledge.
>
> * * *
>
> Senator GURNEY: . . . I think a judge could own something in Western, which is one of the conglomerates and they are buying and selling all of the time, and he could fall afoul of that not really knowing what he owned at any one time, as far as a subsidiary is concerned. So, what I am saying, is I think we have a real problem here. We are going to have a problem.

Senate Hearings at 38.[7] The point was raised again with Professor Frank, who helped draft the Bayh bill:

> MR. FRANK: [W]e also have to keep in mind the point Senator Gurney made in the colloquy with Senator Bayh, and that is we do not want to clog judicial administration by having mistakes turn up later that require retrials or anything of that sort. And there is a limit to what the judge can do.

Senate Hearings at 36. Thus Congress, in adopting the Burdick bill recognized the significance of the knowledge requirement found in Section 455(b)(4), yet the Davis Family would have this Court read that requirement out of the law by adopting a position that has never before been accepted by any court — that the combination of Section 455(b)(4) and Section 455(c) creates a conclusive presumption of knowledge.

There is no basis in the legislative history for such a reading. Nor does such a reading create the "objective test" that the Davis Family claims it does. Petition, p. 18. Conclusive presumptions are not "tests" at all; they are procedural devices that eliminate the need for fact-finding. The objective test instead asks what reasonable persons would conclude from the circumstances. *See, e.g., Boleman v. Congdon and Carpenter Co.*, 638 F.2d. 2, 4 (1st Cir. 1981) (In the context of formation of a contract, a binding offer is made when the offeror leads the offeree reasonably to believe one has been made). As the Ninth Circuit said:

> The right course under § 455(b) as under § 455(a) is to proceed on a case by case basis, determining the

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[7] The Davis Family notes that this Court has not ruled whether the ownership of the stock of the corporate parent of a party is ownership of a financial interest of a party. Petition, p. 7. Bankruptcy Judge McGuire best characterized this, however, as "a nonissue," Pet. App. 21, and it is not implicated by the petition. No one seriously contests that given that the overwhelming majority of J. P. Morgan's business is the ownership of the Morgan Guaranty Bank, once the relationship was discovered by the judge, disqualification was warranted under § 455(a) even if not under § 455(b)(4). While there might have been a question whether the parties could have agreed to let Judge McGuire dispose of his stock and continue in the case, *see* 28 U.S.C. § 455(e), Judge McGuire eliminated that potential issue by voluntarily recusing himself.

> existence of disqualifying knowledge at the time the judge sat, *in the way that a state of mind is normally determined, from inspection of all the circumstances.*

Davis v. Xerox, 811 F.2d at 1296 (emphasis supplied).

Nowhere does the legislative history suggest any Congressional intent to depart from this normal test for knowledge. Even the statement of Professor Frank quoted by the Davis Family — "they will not be excused from failing to know what they have" — does not unambiguously express an intent to depart from the normal objective test for determining knowledge. Petition, p. 15, citing Senate Hearings at 115.[8] In addition, Professor Frank's testimony helps to put his prepared statement in perspective. Even he acknowledged that "there is a limit to what the judge can do." Senate Hearings at 36. Also, in the discussion of the desirability of a knowledge standard, this exchange took place:

> Senator BURDICK: Why do we not follow the pure rule in regard to direct parent companies and apply the knowledge rule to the subsidiaries? Would that not take care of it?
>
> MR. FRANK: It would; and it might well be a good solution so long as at least you could not remove some duty on the part of the judge to be informed. In other words, you could not have a fellow *utterly neglecting* to find out.

Senate Hearings at 44. (emphasis supplied).

Section 455(c) does not create a conclusive presumption of knowledge. In fact, it says nothing about what a judge actually or presumably knows. Nor does it state a mandatory duty of the judge to ascertain everything possible about his holdings. It merely directs the judge that he "*should* inform himself," 28 U.S.C. § 455(c) (emphasis supplied), and precludes the use of

[8] The quoted remarks come not from Professor Frank's live testimony, but from his prepared statement, which was neither discussed nor explicitly adopted by any member of Congress.

a blind trust to avoid disqualification. *See NEC Corp.*, 654 F.Supp. at 1258 n.2.

Particularly in light of the Congressional debate on whether to adopt a knowledge requirement, meaning must be given to the different words Congress selected: "know," "shall" and "should." *See Reiter v. Sonotone Corp.*, 442 U.S. 330, 338-339 (1979) (in construing a statute, courts are obliged to give effect, if possible, to every word Congress used). Here subsections (b)(4), (b)(5)(iii) and (b)(5)(iv) of Section 455 require knowledge by the judge; the other subsections do not. Where Congress includes particular language in one section of a statute, but omits it in another section of the same act, it is generally presumed that Congress acted intentionally and purposely in so doing. *Russello v. United States*, 464 U.S. 16, 22-23 (1983). Comparing the various subsections of Section 455, Congress' intent and purpose becomes clear. Congress included a knowledge requirement whenever it perceived that an absolute rule would raise substantial practical difficulties. Similarly, Congress' selection of "should" in Section 455(c) instead of "shall" as in Sections 455(a) and (b) suggests that Congress intended to articulate mandatory duties in Sections 455(a) and (b), but not in Section 455(c).

The Davis Family simply seeks to blur the distinctions among the various subsections of Section 455, so as to read into one part of the statute useful language from another. This the Davis Family cannot do, for under accepted rules of statutory construction, each word must be given meaning, and clearly different words should not be given the same meaning.

Due Process Does Not Require the Interrogation Of Bankruptcy Judge McGuire

The Davis Family also suggests that the decision below conflicts with existing law requiring a due process hearing. Judge McGuire's prompt disclosure of his discovery of his interest, however, enabled the Davis Family to receive a due

process hearing. The District Court considered the Davis Family's arguments concerning Section 455 on their merits and rejected them. The Fifth Circuit considered an emergency motion for stay and denied it. Finally, the Fifth Circuit reviewed, and affirmed, the District Court's decision. The only conceivable question is whether the District Court erred in quashing the notice of Bankruptcy Judge McGuire's deposition.

Traditionally the trial court is given wide latitude in controlling the scope of discovery, and its decisions are reviewed under the abuse of discretion standard. *See, e.g., O'Neal v. Riceland Foods*, 684 F.2d 577 (8th Cir. 1982) (district court has wide discretion in its handling of discovery matters; its decisions are to be upheld unless, in the totality of the circumstances, its rulings constitute such a gross abuse of discretion as to result in fundamental unfairness). On review, the Fifth Circuit found no basis for questioning Bankruptcy Judge McGuire's statements in his judicial capacity. Pet. App. 7.

Unless due process is to require the unseemly interrogation under oath of every judge who, discovering information new to him, advises the parties and seeks to cure any potential disqualification problems, there is no call for certiorari here. The district court in *NEC Corp.*, rejecting arguments similar to those advanced here by the Davis Family,[9] recognized the significant problems of such an "inquisition into the judge's state of mind." As observed by the *NEC* court:

> This inquiry might entail deposing, examining, cross-examining, and impeaching the judge and might

[9] NEC Corporation and the Davis Family both filed *amicus curiae* briefs in *Liljeberg v. Health Services Acquisition Corp.*, (No. 86-957), argued December 9, 1987, urging the adoption of a conclusive presumption rule. See Brief of Amici Curiae Kenneth W. Davis, Jr., et al., *Liljeberg*, (No. 86-957), filed July 23, 1987; Brief of Amici Curiae NEC Corporation and NEC Electronics, Inc. in Support of Respondent Health Services Acquisition Corp., *Liljeberg*, (No. 86-957), filed July 22, 1987.

> require another judge to make findings of fact on a colleague's credibility. NEC is correct in arguing that this "unseemly procedure" . . . would do little to advance the statutory purpose to "promote public confidence in the impartiality of the judicial process," House Report, . . . at 1974 U.S. Code Cong. & Admin. News 6357, and should be avoided.

NEC Corp., 654 F.Supp. at 1258. In the instant case, Judge McGuire, by coming forward, and by recusing himself, has already best promoted public confidence in the impartiality of the judicial process.

Vacating Bankruptcy Judge McGuire's Orders Would Demean, Not Promote, The Image of the Federal Judiciary.

The practical effect of vacating Bankruptcy Judge McGuire's orders may well be the liquidation of Kendavis Holding Company, which recently emerged from over two years of bankruptcy proceedings during which Judge McGuire issued hundreds of orders and the estate paid over 20 million dollars in professional fees. R. App. 24. Given that prior to the implementation of the confirmed plan, KHC was insolvent, it is highly doubtful that the company could survive another journey through the bankruptcy process. Yet the relief sought would require just that — even the Orders for Relief were entered by Judge McGuire and, under the Davis Family's theory, would be vacated.

It is simply not plausible that the thousands of creditors and other persons affected by Judge McGuire's orders, or the public at large, would find any justice if the Davis Family were able, in the absence of any showing of actual bias or impartiality, to thwart the entire reorganization process. In the first place, the Davis Family, as shareholders of an admittedly insolvent corporation, lacked standing to challenge the Bankruptcy Court's orders on their merits. *See, e.g., In re Dutch Inn of Orlando, Ltd.*, 614 F.2d 506, 508 (5th Cir. 1980) (limited partners of insolvent limited partnership lacked standing). Second, the fact that some members of the Davis Family may

previously have been the principal officers and directors of KHC does not grant them any independent standing. *See, e.g., In re Johns-Manville Corp.*, 801 F.2d 60, 65 (2d Cir. 1986). Third, the substantive challenges to the confirmed plan that the Davis Family did assert were meritless. The Fifth Circuit found them to be "frivolous." Pet. App. 7.

From a broader perspective, much of the public's confidence and faith in the judiciary stems from the finality of judicial decisions. If the Davis Family's position were to be accepted, any creditor or other person dealing with an entity operating under the protection of the Bankruptcy Code would have to live with the fear that even the simplest, most benign, mistake by the judge could void every action taken during the course of the proceedings. Particularly when bankruptcies may involve thousands of creditors, the potential for innocent oversight is great, and the practical effect of the Davis Family's rule may be the wholesale recusal of all bankruptcy judges who own securities of individual corporations. "Such broad-scale disqualification is an unlikely purpose to impute to Congress in passing section 455(b)." *Union Carbide Corp.*, 782 F.2d at 715 (discussing the problems of unidentified corporate class members). Also, broad-scale disqualification and retrospective recusal are hardly the practical, easy-to-implement, solution sought by Congress in drafting Section 455. They are, instead, precisely what troubled Professor Frank when he testified that "we do not want to clog judicial administration by having mistakes turn up later that require retrials or anything like that." Senate Hearings at 36.

Judge McGuire's Orders Should Not Be Vacated Because The Appeal of the District Court's Denial of the Motions to Vacate Has Been Rendered Moot

Although the KHC entities, under former management, repeatedly sought a stay of the implementation of the confirmed plan, no stay was ever issued to bar the implementation of the plan on its Effective Date, April 16, 1987. Accordingly,

the confirmed plan became effective on April 16, 1987, and since that time, KHC (under its new management as provided for by the plan) has taken numerous steps to implement the confirmed plan. Many of these steps are detailed in the Amended Affidavit of David E. Hawthorne, which was filed with the Fifth Circuit.[10] As even the Davis Family conceded before the Fifth Circuit, the effect of these steps is the "substantial consummation" of the confirmed plan. *See* 11 U.S.C. § 1101(1) (1982).

Just as Congress was mindful when drafting 28 U.S.C. § 455 of the needs for finality of judicial decisions and efficient administration of the judicial system, so also was it mindful that absent a stay pending appeal, parties involved in a bankruptcy case must be able to rely upon the finality of a court's orders.[11]

The circuit courts are nearly unanimous in applying the mootness doctrine in the bankruptcy context to require dismissal of challenges to a confirmed plan of reorganization that has been so substantially implemented that effective judicial relief is no longer available to the appellant, even if the appeal were to be decided in its favor. *See, e.g., In re AOV Industries, Inc.*, 792 F.2d 1140 (D.C. Cir. 1986); *In re Sun Country Development, Inc.*, 764 F.2d 406 (5th Cir. 1985); *In re Information Dialogues, Inc.*, 662 F.2d 475 (8th Cir. 1981). Indeed, the practical needs in Chapter 11 proceedings for creditors, debtors and non-parties to rely on the finality of a debtor's court-approved actions are such that, as the Ninth Circuit stated in a pre-Code case, "reversal of [an] order confirming the plan of arrangement, which would knock the

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[10] The Amended Affidavit is reprinted at R. App. 12-24.

[11] This need was recognized by Congress in relation to sales of assets. Section 363(m) of the Bankruptcy Code provides that an order authorizing use, sale or lease of a debtor's property is final, even if the order has been reversed on appeal, unless the appellant obtains a stay pending the appeal. 11 U.S.C. § 363(m) (1982). Courts have applied the same analysis to appeals from orders confirming a plan of reorganization. *See generally* Broude, Reorganizations Under Chapter 11 of the Bankruptcy Code, § 14.01[1] (1986).

props out from under the authorization for every transaction that has taken place, would do nothing other than create an unmanageable, uncontrollable situation . . .." *In re Roberts Farms*, 652 F.2d 793, 797 (9th Cir. 1981).

Most recently, the Eleventh Circuit held that when a confirmed plan has been substantially consummated and all creditors either have been paid or have had sufficient monies reserved to pay their claims if allowed, an appeal of the confirmation of the plan is moot. *Miami Center Limited Partnership v. Bank of New York*, 820 F.2d 376 (11th Cir.), *modified on other grounds*, 826 F.2d 1010 (1987). This is precisely the case here. Virtually all required corporate actions have been taken, KHC has paid in full the holders of allowed Class 1 through 6 claims, and stock and notes have been issued to the holders of Class 7 claims. Only holders of Class 7 claims, who are now the shareholders of KHC, await receipt of cash distributions. R. App. 12-24. Since all classes have received payment or other distributions, vacating the Confirmation Order, and the hundreds of Judge McGuire's other orders, would serve no useful purpose. It would simply reinstate the former shareholders of acknowledged insolvent debtors, and wreak havoc upon the affairs of hundreds of creditors. Accordingly, the controversy is moot.

CONCLUSION

For the reasons stated above, this Court should dismiss or deny the petition for writ of certioriari.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Brett A. Ringle, counsel of record for Respondent Kendavis Holding Company and a member of the Bar of the Supreme Court of the United States, hereby certify that I have served three copies of Respondent Kendavis Holding Company's Brief in Opposition to Petition for Writ of Certiorari and the Joint Appendix to Briefs in Opposition of Respondents Kendavis Holding Company and the Official Unsecured Creditors' Committees on all parties required to be served, by depositing three copies of each in the United States mail, on this

20th day of December, 1987, with first class postage prepaid, addressed to the listed counsel of record at the addresses indicated.

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CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

IN RE KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., .

Debtors

K.W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A," A. T. DAVIS, A. T. DAVIS TRUST "A," KAY DAVIS, KAY DAVIS TRUST "A," TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A. T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T. C. DAVIS, II, T. C. DAVIS, II TRUST, T. C. DAVIS, II TRUST "A," T. C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A," BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T. C. DAVIS,

Petitioners

V.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC. AND LOFFLAND BROTHERS COMPANY, KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

JOINT APPENDIX TO BRIEFS IN OPPOSITION OF RESPONDENTS KENDAVIS HOLDING COMPANY AND THE OFFICIAL UNSECURED CREDITORS' COMMITTEES

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IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE: KENDAVIS HOLDING COMPANY, ET AL., *Debtors/Appellants.*	CIVIL ACTION NO. CA 3-86-2995-G

MEMORANDUM ORDER

This case is before the court on appeal from orders and related findings of the Bankruptcy Court confirming a creditor plan of reorganization, denying a debtor plan of reorganization, and denying a new trial as to the debtor plan of reorganization.

I. Parties

The appellants include Kendavis Holding Company ("KHC"), Kendavis Industries International, Inc. ("KIII"), Loffland Brothers Company ("Loffland"), Mid-Continent Supply Co. ("Mid-Continent"), Geodril, Inc. ("Geodril"), Loffland Brothers Eastern Hemisphere, Inc. ("LBEH"), Loffland Brother (Singapore) PTE., Ltd. ("LBS"), Cummins Sales and Service, Inc. ("Cummins"), Frigette Corporation, Inc. ("Frigette"), Globe Machinery and Supply Company ("Globe"), Harrisburg, Inc. ("Harrisburg"), Kendavis Industrial Supply Co. ("KISCO"), Mechanical Rubber Products Corporation ("Mechanical Rubber"), Miami-Dickerson Steel Company ("Miami-Dickerson"), Midco Equipment Co. ("Midco"), Moore & Sons, Inc. ("Moore"), Rig-A-Lite Company, Inc. ("Rig-A-Lite"), Sligo, Inc. ("Sligo"), State Pipe & Supply Co. ("State Pipe"), and Unit Rig & Equipment Co.

("Unit Rig"). Appellees are the Official Unsecured Creditors' Committees for KHC, KIII and Loffland ("the Committees") and various other creditors.

II. Procedural Background

The underlying chapter 11 bankruptcy cases of KIII and KHC commenced on February 21, 1985 when eight unsecured institutional creditors owed in excess of $440,000,000.00 filed involuntary petitions for relief. KIII and KHC consented to the filings, and orders for relief were entered on March 19, 1985. Loffland filed a voluntary petition for relief under chapter 11 on March 17, 1985.

On August 6, 1986, the Bankruptcy Court issued an order denying confirmation of the Debtors' Third Amended Joint Plan of Reorganization (the "Debtors' Plan").[1] The Debtors filed a motion for new trial which was denied on November 24, 1986.

On November 24, 1986, the Bankruptcy Court confirmed the Committees' Plan as to KHC and KIII but denied confirmation of the stand-alone portion of the Committees' Plan relating to Loffland.

The appellants assert various defects in the Committees' Plan which, they maintain, make the plan unconfirmable. In addition, they raise questions of jurisdiction and challenge the order denying confirmation of the Debtors' Plan. Appellees have moved to dismiss the appeals for lack of standing.

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[1] The Debtors' Plan was also filed by KIII, KHC and Loffland. It was also jointly proposed by Mid-Continent, Geodril, LBEH, and LBS, each of which either consented to orders for relief in then pending involuntary cases or filed voluntary petitions for relief under chapter 11. The cases of KIII, KHC, Loffland, Mid-Continent, Geodril, LBEH and LBS have subsequently been administered jointly under Case No. 385-30348-M-11. The seven debtor proponents of the Debtors' Plan are sometimes referred to collectively as the "Debtors."

III. Standing

Appellants have raised forty-three issues for consideration on this appeal. *See* Brief of Appellants, pp. 2-7. They have standing, however, to challenge only those parts of the reorganization plan that affect their direct interests. In re Johns-Manville Corporation, 68 Bankr. 618, 623 (Bankr. S.D. N.Y. 1986); In re Evans Products Company, 65 Bankr. 870, 874 (S.D. Fla. 1986); In re Sweetwater, 57 Bankr. 743, 746 (D. Utah 1985). To have standing to appeal, the appellant must be an aggrieved person, directly, adversely, and pecuniarily affected by the order of the Bankruptcy Court. *In re Sweetwater,* above, 57 Bankr. at 746; Holywell Corporation v. Bank of New York, 59 Bankr. 340, 349-50 (S.D. Fla. 1986).

The court is of the opinion that Loffland has no standing to appeal confirmation of the Committees' Plan. The Committees' Plan contained a stand-alone plan of reorganization for Loffland, which was denied in the order of confirmation. Loffland is not aggrieved by denial of the Committees' stand-alone plan for Loffland or by confirmation of the remainder of the Committees' Plan.

KHC and KIII are insolvent. This insolvency is an insurmountable threshold which denies standing to KHC and KIII to assert any issue on appeal. Matter of Dutch Inn of Orlando, Ltd., 614 F.2d 506, 507-08 (5th Cir. 1980); Matter of Fondiller, 707 F.2d 441, 442 (9th Cir. 1983); *In re Evans Products Co.,* above, 65 Bankr. at 874; Matter of Snyder, 56 Bankr. 1007, 1011 (N.D. Ind. 1986); *Holywell Corporation v. Bank of New York,* above, 59 Bankr. at 349-50; *In re Sweetwater,* above, 57 Bankr. at 746-47. The court is therefore of the opinion that KHC and KIII are not aggrieved persons and do not have standing to appeal the confirmation of the Committees' Plan.

The court is also of the opinion that the subsidiary corporations[2] lack standing to appeal confirmation of the Committees' Plan. After the Committees' Plan was modified, the time for filing objections to it was extended until May 12, 1986. No objections on behalf of the subsidiary corporations were filed by May 12, 1986. Although the subsidiary corporations did file late objections to perceived asset transfers only, no leave was sought below to file them out of time. This court will not consider issues not properly presented to, and decided by, the court below. *See* In re Modern Boats, Inc., 775 F.2d 619, 621 (5th Cir. 1985); Masat v. United States, 745 F.2d 985, 988 (5th Cir. 1984).

Moreover, the actual objections raised as to the perceived asset transfers are premature. No transfers from the subsidiary corporations to KHC or KIII have yet been presented to the Bankruptcy Court, and none has been approved. Thus, the issue of perceived asset transfers is not ripe for appeal.

The court is of the further opinion that the Davis Family,[3] as shareholders of KHC, are not aggrieved persons and have no standing to appeal. Since their interests in KHC are without value, they have no stake in these appeals as shareholders. *See, e.g., In re Evans Products Co.*, above, 65 Bankr. at 874-75.

K.W. Davis, Jr., T.C. Davis and Kay Davis have class 6 creditor claims. All three voted to reject the Committees' Plan.

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[2] Mid-Continent, Geodril, LBEH, LBS, Cummins, Frigette, Globe, Harrisburg, KISCO, Mechanical Rubber, Miami-Dickerson, Midco, Moore, Rig-A-Lite, Sligo, State Pipe and Unit Rig.

[3] Collectively, Kenneth W. Davis, Jr. and T. Cullen Davis, Alana Lawler, Alana Lawler Trust "A," A.T. Davis Trust "A," Kay Davis, Kay Davis Trust "A," Tricia Kae Lawler, Alana Lawler's Children's Trust, Allen Kenneth Davis, Janiece Breanne Davis, A.T. Davis Children's Trust, Kay Davis Children's Trust, T.C. Davis, II, T.C. Davis, II Trust, T.C. Davis, II Trust "A," T.C. Davis, II Trust "A" dated January 15, 1982, Chesley Davis, Chesley Davis Trust, Trey Davis, Trey Davis Trust, and Ken W. Davis Foundation.

As creditors, these three Davises would normally have standing to appeal. In this case, however, not a single member of the Davis Family, as either shareholder or creditor, made an appearance at the confirmation hearings on the Committees' Plan or filed written objections, as contemplated by Bankruptcy Rule 3020 and as required by the Bankruptcy Court in this case. All of the Davis Family had notice of such hearings. Voting to reject the Committees' Plan did not, alone, preserve what standing K.W. Davis, Jr., T.C. Davis and Ray Davis [sic] might have had to appeal. None of the Davis Family members have a right to be heard for the first time on appeal. *See* Bankruptcy Rule 3020; In re Neff, 60 Bankr. 448, 457-58 (Bankr. N.D. Tex. 1985); In re Sweetwater, 57 Bankr. 748, 750 (D. Utah 1985) (*Sweetwater II*); In re Record Club of America, 38 Bankr. 691, 696-97 (M.D. Pa. 1983).

IV. Conclusion

For the foregoing reasons, this court concludes that KHC, KIII, Loffland, the subsidiary corporations, and the Davis Family do not have standing to attack the Committees' Plan on appeal. Appellees' motion to dismiss is thus GRANTED in part, and the appeals by these parties from confirmation of the Committees' Plan are DISMISSED.

At no time, however, do the appellees argue persuasively that the Debtors lack standing to take an appeal from denial of confirmation of the Debtors' Plan. Instead, the appellees urge that consideration of a plan other than the Committees' Plan is precluded. The court disagrees. It might be determined that the Debtors' Plan is confirmable and that these cases should be remanded to the Bankruptcy Court for a determination as to which plan to confirm. 11 U.S.C. §1129(c).

Accordingly, the merits of the Debtors' Plan is considered in a separate memorandum order. Appellees' motion to dismiss

is DENIED in part as to the alleged mootness of any consideration of the Debtors' Plan.

SO ORDERED.

March 26, 1987.

/s/ A. Joe Fish

A. JOE FISH
United States District Judge

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

OFFICIAL SHAREHOLDERS COMMITTEE OF MID-CONTINENT SUPPLY CO.,
Plaintiff,

vs.

KENDAVIS HOLDING CO., ET AL.,
Defendants.

CIVIL ACTION NO.
CA 3-86-3108-G

ORDER

This case is before the court on appeal of the Official Shareholders Committee of Mid-Continent Supply Company ("Mid-Continent Shareholders Committee") from an order and related findings of the Bankruptcy Court, which confirmed a creditor plan of reorganization for Kendavis Holding Company ("KHC") and Kendavis Industries International, Inc. ("KIII"). Mid-Continent Supply Company ("Mid-Continent") is a subsidiary of KHC.

The Mid-Continent Shareholders Committee does not represent any interest of creditors or shareholders of KHC or KIII, or any creditor of Mid-Continent. Rather, it represents only the interests of owners of Class B stock of Mid-Continent. The court is of the opinion that the Mid-Continent Shareholders are not aggrieved parties with respect to the confirmation of the Committees' Plan. *See, e.g.*, In re Evans Products Co., 65 Bankr. 870, 874 (S.D. Fla. 1986), In re Snyder, 56 Bankr. 1007, 1011 (N.D. Ind. 1986); Holywell Corporation v. Bank of New York, 59 Bankr. 340, 349-50 (S.D. Fla. 1986); In re Sweetwater, 57 Bankr. 743, 746-47 (D. Utah 1985); Matter of Dutch Inn of Orlando, Ltd., 614 F.2d 506, 507-08 (5th Cir. 1980).

Accordingly, the motion to dismiss the appeal of the Mid-Continent Shareholders Committee is GRANTED and the appeal of the Mid-Continent Shareholders Committee is DISMISSED.

SO ORDERED.

March 26, 1987.

/s/ A. Joe Fish

A. JOE FISH
United States District Judge

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE: KENDAVIS HOLDING COMPANY, ET AL., *Debtors/Appellants.*	CIVIL ACTION NO. CA 3-86-2995-G

ORDER

Appellants have filed a joint motion for an expedited appeal and determination that the Modified Joint Plan of Reorganization ("Committees' Plan") for debtors Kendavis Holding Company ("KHC") and Kendavis Industries International, Inc. ("KIII") cannot be implemented. Appellants have, alternatively, filed a joint motion for stay pending appeal. For the reasons set forth in this court's memorandum order of March 26, 1987, which granted, in part, appellees' motion to dismiss, this court is of the opinion that appellants do not have standing to pursue appeals of the confirmation of the Committees' Plan. Accordingly, appellants' joint motion for expedited appeal and determination that the Committees' KIII/KHC Plan cannot be implemented is DENIED. Appellants' joint motion for stay pending appeal is also DENIED.

SO ORDERED.

March 26, 1987.

/s/ A. Joe Fish

A. JOE FISH
United States District Judge

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE: KENDAVIS HOLDING COMPANY, ET AL., *Debtors/Appellants.*	CIVIL ACTION NO. CA 3-86-2995-G

JUDGMENT

This cause came on to be heard on the record on appeal and taken under submission on the briefs on file.

On consideration whereof, it is now here ORDERED and ADJUDGED by this court that the order of the Bankruptcy Court appealed from in this cause is AFFIRMED.

It is further ORDERED that debtors/appellants pay to creditors/appellees the costs on appeal, to be taxed by the clerk of this court.

March 26, 1987.

/s/ A. Joe Fish

A. JOE FISH
United States District Judge

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE: KENDAVIS HOLDING COMPANY, ET AL., *Debtors/Appellants.*	CIVIL ACTION NO. CA 3-86-2995-G

ORDER

The Davis family have filed a motion to join the corporate appellants' implementation motion. The motion to join is DENIED.

SO ORDERED.

March 26, 1987.

/s/ A. Joe Fish

A. JOE FISH
United States District Judge

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

Case No. 87-1251

In re KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC., LOFFLAND BROTHERS COMPANY, MID-CONTINENT SUPPLY CO., GEODRIL INC., LOFFLAND BROTHERS EASTERN HEMISPHERE, INC., AND LOFFLAND BROTHERS (SINGAPORE) PTE. LTD.,

Debtors,

KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC., LOFFLAND BROTHERS COMPANY, MID-CONTINENT SUPPLY CO., GEODRIL INC., LOFFLAND BROTHERS EASTERN HEMISPHERE, INC., AND LOFFLAND BROTHERS (SINGAPORE) PTE. LTD., CUMMINS SALES & SERVICE, INC., FRIGETTE CORPORATION, GLOBE MACHINERY & SUPPLY COMPANY, HARRISBURG, INC., KENDAVIS INDUSTRIAL SUPPLY CO., MECHANICAL RUBBER PRODUCTS CORPORATION, MIAMI-DICKERSON STEEL COMPANY, MIDCO EQUIPMENT CO., MOORE & SONS, INC., RIG-A-LITE COMPANY, INC., SLIGO, INC., STATE PIPE AND SUPPLY CO., AND UNIT RIG & EQUIPMENT CO.,

Appellants,

VS.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC., AND LOFFLAND BROTHERS COMPANY,

Appellees.

AMENDED AFFIDAVIT OF DAVID E. HAWTHORNE

DAVID E. HAWTHORNE, being first duly sworn, deposes and says:

1. I am currently Secretary of the Kendavis Holding Company ("KHC") and a director and officer of KHC and various KHC subsidiaries. I have served as an officer of KHC and its wholly owned subsidiaries since April 16, 1987 and have served as an officer and director of certain other KHC subsidiaries since May 1, 1987.

2. I have personal knowledge of the events and actions described below, all of which were taken to implement the Official Unsecured Creditors' Committee's Modified Joint Plan of Reorganization for KHC and Kendavis Industries International, Inc. the ("Confirmed Plan") or otherwise in the conduct of the business of KHC and its subsidiaries on or after April 16, 1987, the effective date of the Confirmed Plan (the "Effective Date").

SUMMARY OF THE BUSINESS AND STRUCTURE OF THE KHC COMPANIES

3. KHC is a Nevada corporation. The principal assets of KHC consist of the stock of its subsidiaries. Prior to its merger into KHC on the Effective Date, Kendavis Industries International, Inc. ("KIII") was a Texas corporation that provided financial, management and other services to the various KHC subsidiaries, which subsidiaries are engaged in a variety of businesses ranging from contract drilling and related oil field services to the manufacture and sale of heavy equipment. Subsequent to KIII's merger into KHC on the Effective Date, KHC has provided management services to the KHC subsidiaries. Except for KIII, which no longer exists, all of the KHC Appellants, as that term is defined in the Brief in Support of Motion of the KHC Appellants to Dismiss Their Appeal and the Appeal of the Davis Family Appellants, are direct or indirect subsidiaries of KHC. KHC is the principal or sole

shareholder of each of its direct subsidiaries. Certain of these direct subsidiaries also own all or substantially all of the outstanding stock of other corporations (second tier subsidiaries) which, in turn, own all or substantially all of the outstanding stock of other corporations (third tier subsidiaries).

4. Until the Effective Date, all of the stock of KHC was owned by members of the Davis family. Members of the Davis family also served as the principal management of KHC and its subsidiaries. Kenneth W. Davis, Jr. was Chairman of the Board and President of KHC; T. Cullen Davis was Vice President of KHC and Kay Davis was Secretary of KHC. In addition, each of KHC's direct subsidiaries had at least one member of the Davis family as an officer and director of such corporation.

5. Amended Articles of Incorporation for KHC were filed on the Effective Date in the office of the Secretary of State of Nevada. All previously outstanding shares of stock of KHC (all of which were held by the Davis Family) were cancelled, and new common and preferred stock ("KHC Common and Preferred Stock") to be issued pursuant to Confirmed Plan to holders of KIII-7/KHC-7 allowed claims (the "Class 7 Claims") was authorized.

6. On the Effective Date, KIII was merged into KHC as required by the terms of the Confirmed Plan and in accordance with applicable corporate laws of the States of Nevada and Texas. Certificates of Merger were filed with the Secretaries of State of Nevada and Texas, upon which the separate corporate existence of KIII ceased and KHC succeeded to all of KIII's assets and liabilities.

PAYMENTS AND DISTRIBUTIONS UNDER THE PLAN

7. Pursuant to the Confirmed Plan, an aggregate of 3,574,639 shares of KHC Common Stock and 1,191,546 shares of KHC Preferred Stock was issued in respect of allowed Class 7 Claims under the Confirmed Plan on the Effective Date. As a result of the resolution of previously contested Class 7 Claims, through September 9, 1987, an aggregate of an additional 5,335,369 shares of KHC Common Stock and 1,778,458 shares of KHC Preferred Stock have been issued to holders of Class 7 Claims since the Effective Date. There are now 26 holders of KHC Common and Preferred Stock. The current holders are: American Bank & Trust Co., The Bank of New York, The Bank of Nova Scotia, Bank of Oklahoma, N.A., The Chase Manhattan Bank, N.A., Credit Commercial de France (New York Branch), Den Norske Creditbank, Continental Illinois National Bank and Trust Company of Chicago, as Administrator for the Federal Deposit Insurance Corporation, Federal Deposit Insurance Corporation, in its corporate capacity, First City National Bank of Fort Worth, First City National Bank of Houston, First Interstate Bank of California, C.S.M., Inc., InterFirst Bank Fort Worth, N.A., Irving Trust Company, Marine Midland Bank, N.A., City Investment Company, Morgan Guaranty Trust Company of New York, Sanwa Bank California, Seattle First National Bank, Security Pacific National Bank, Texas American Bank/Fort Worth, N.A., Beta Development Co., Mechanical Rubber Products Corporation, Miami-Dickerson Steel Company and Sligo, Inc. The remaining authorized but unissued KHC Common and Preferred Stock, aggregating 89,992 shares and 29,996 shares, respectively, is reserved for issuance to holders of Class 7 Claims upon resolution of the remaining disputed claims.

8. Pursuant to the Confirmed Plan, KHC Long Term Notes in the aggregate principal amount of $49,647,756.22, and

KHC Short Term Notes in the aggregate principal amount of $15,887,281.98 were issued in respect of allowed Class 7 Claims under the Confirmed Plan on the Effective Date. As a result of the resolution of previously contested Class 7 Claims through September 9, 1987, an additional aggregate principal amount of $74,102,374.93 of KHC Long Term Notes and $23,712,760.00 of KHC Short Term Notes have been issued to holders of Class 7 Claims since the Effective Date. Again, there are 26 holders, as identified in paragraph 7 above, of KHC Long Term Notes and KHC Short Term Notes, and additional KHC Long Term Notes and KHC Short Term Notes, in an aggregate principal amount of $1,249,868.85 and $399,958.02, respectively, will be issued as disputed claims are resolved.

9. Through September 9, 1987, KHC has made distributions of Available Cash, as defined in the Confirmed Plan, in respect of allowed Class 7 Claims in an aggregate amount of $39,600,041.98. In connection with these distributions, an aggregate of $399,958.02 is reserved for future distribution upon resolution of the four remaining disputed Class 7 Claims described in paragraph 11 below.

10. On July 16, 1987, KHC paid its first regular interest payment in respect of the KHC Long Term Notes and Short Term Notes issued pursuant to the Confirmed Plan. As a result of the subsequent allowance of previously contested Class 7 Claims through September 9, 1987, an aggregate of $4,754,755.04 has been paid in interest on such notes and $48,022.74 is reserved for payment in respect of the four remaining disputed Class 7 Claims.

11. As of the date hereof, only four Class 7 Claims, aggregating $5,236,424.57, remain disputed. Assuming all of these remaining disputed Claims are allowed, they represent less than one percent of the total allowed Class 7 Claims.

12. As required by the Confirmed Plan, through September 9, 1987 cash payments in an aggregate amount of

$1,541,531.15 were made to 43 holders of allowed KIII-1/KHC-1 through KIII-5/KHC-5 Claims, and the balance of the holders of Claims in these classes had their rights reinstated, thereby representing full satisfaction of such allowed claims.

13. As required by the Confirmed Plan, nine holders of allowed KIII-6/KHC-6 claims (the "Class 6 Claims") were paid aggregate of $293,651.69 on the Effective Date. These amounts included the payment of installments of allowed Class 6 claims to Kenneth Davis of $8,312.86 and Kay Davis of $2,942.67. Kay Davis has an allowed Class 6 Claim of $8,828. The business records of KHC, however, indicate that by check dated April 11, 1985, while KHC and KIII remained debtors in possession, Kay Davis was paid $8,900 by KIII, which, according to KHC records and employees, constituted an advance in respect of the same expenses as constitute her claim.

14. In May 1987, KHC filed a motion with the Bankruptcy Court to accelerate and prepay the remaining $493,964.96 (plus accrued interest from the Effective Date) owed to holders of allowed Class 6 Claims and to reserve a total of $99,080.00 for the holders of disputed Class 6 Claims. At a hearing postponed from June 8, 1987 and held on August 28, 1987, the Bankruptcy Court ordered (and confirmed on September 4, 1987 at a further conference) that KHC be permitted to prepay such Class 6 Claims after 48 hours following oral arguments to the Fifth Circuit, currently scheduled for September 16, 1987. KHC intends to make such payments as permitted by the Bankruptcy Court.

15. On August 14, 1987, the Bankruptcy Court disallowed approximately 120 previously contested employee wage claims aggregating approximately $300,000, representing substantially all of the remaining contested Class 1, Class 5 and Class 6 Claims. Remaining disputed claims in those Classes are scheduled for hearing on October 19, 1987.

16. Pursuant to Claims resolutions described in foregoing paragraphs, there are approximately 16 contested Claims

remaining to be resolved aggregating in face amount approximately $5.5 million, excluding certain continuing disputes relating to professional fees.

CHANGES IN MANAGEMENT

17. Pursuant to the Confirmed Plan and Amended Articles of Incorporation, the former board of directors of KHC (composed of Kenneth Davis, T. Cullen Davis and Kay Davis) was removed and a new board of directors of KHC was appointed consisting of Joe B. Freeman, L. E. Simmons and Francis L. Durand. Subsequently, L. E. Simmons resigned from the board and I was elected to fill the vacancy created by his resignation.

18. On the Effective Date, all former officers of KHC were removed and the following officers were elected by the newly constituted board of directors of KHC:

Name	Office
Joe B. Freeman.....	Chairman of the Board, President and Chief Executive Officer
David E. Hawthorne	Vice President, Secretary and Treasurer

On the Effective Date, the new board of directors of KHC approved a three-year employment agreement with Joe B. Freeman and a letter agreement with respect to my own employment.

19. Also on the Effective Date, KHC, as the sole shareholder of the following six subsidiaries (three of which are KHC Appellants in the KHC Appeal), among other things, removed the existing boards of directors and elected new boards of directors for such subsidiaries (the "Wholly Owned Subsidiaries") in accordance with the respective corporate law

of the states of their incorporation and the respective articles or certificates of incorporation and by-laws of each corporation ("Charter Documents"):

Wholly Owned Subsidiaries	State of Incorporation
Beta Development Co.	Texas
Frigette Corporation	Texas
Geodril Inc.	Nevada
Kimco, Inc.	Texas
Moore & Sons, Inc.	Tennessee
Sierra International, Inc.	Texas

On the Effective Date, pursuant to applicable corporate law and Charter Documents, the boards of directors of each of the Wholly Owned Subsidiaries removed existing officers and elected new officers.

20. Subsequent to the Effective Date, KHC and its subsidiaries, in accordance with applicable corporate law and Charter Documents caused shareholder actions to be taken to remove the directors of each of the following 37 direct or indirect subsidiaries of KHC and, except in the case of Unit Rig & Equipment Co. (South Africa) (Proprietary) Limited, to elect new directors of such subsidiaries (the "Other Subsidiaries"):

Other Subsidiaries	Jurisdiction of Organization
AMC Air Conditioning Company	Texas
Andes Drilling Company	Nevada
CS&S Liquidating Co. (formerly Cummins Sales and Service, Inc.)	Texas
Cummins Sales and Service de Venezuela, C.A.	Venezuela
Cumvenca, Inc.	Texas
Globe Machinery & Supply Company	Iowa
Harrisburg, Inc.	Texas
KECO Limited	Alberta, Canada
Kendavis Industrial Supply Co.	Texas
Loffland Brothers Company	Texas
Loffland Brothers Company of Canada	Delaware

Other Subsidiaries	Jurisdiction of Organization
Loffland Brothers Eastern Hemisphere, Inc. ...	Texas
Loffland Brothers International, Inc.	Delaware
Loffland Brothers North Sea, Inc.	Nevada
Loffland Brothers (Singapore) Pte. Ltd.	Singapore
Mechanical Rubber Products Corporation	Nevada
Miami-Dickerson Steel Company	Ohio
Midco Caribe Co.	Texas
Midco-Chicago Company.....	Illinois
Midco Equipment Co.	Tennessee
Midco Norway Inc.	Nevada
Mid-Continent Supply Co.	Texas
Mid-Continent Supply Eastern Hemisphere Co.	Texas
Mid-Continent Supply Western Hemisphere Co.	Texas
Rig-A-Lite Company, Inc.	Texas
Sligo, Inc.	Nevada
Stair Pipe and Supply Co.	California
Stratoflex, Inc.	Texas
Stratoflex of Canada, Limited	Ontario, Canada
Unit Rig & Equipment Co.	Texas
Cumvenca, C.A.	Venezuela
Loffland Brothers de Venezuela, C.A.	Venezuela
Loffland Brothers (Malaysia) Sdn. Bhd.	Malaysia
Midco Nederland B.V.	The Hague
Nadrico Saudi Limited	Saudi Arabia
Unit Rig & Equipment Co. (Australia) Pty. Limited	Australia
Unit Rig & Equipment Co. (South Africa) (Proprietary) Limited	South Africa

Such new boards of directors have, in certain cases, removed certain of the prior officers of the Other Subsidiaries and elected new officers. Subsequent to such elections, further management changes have been required as a result of the termination of employment of certain management personnel including changes at Loffland Brothers Company, Moore & Sons, Inc. and Unit Rig & Equipment Co.

THE DECISION TO SEEK DISMISSAL OF THE APPEAL

21. Prior to April 29, 1987, the law firm of Locke, Purnell, Boren, Laney & Neely, now Locke Purnell Rain Harrell, ("Locke Purnell") was counsel of record for the KHC Appellants in the bankruptcy proceedings. On April 16, 1987, Jones, Day, Reavis & Pogue ("Jones Day") was retained as counsel for KHC. On April 20, 1987, Joe B. Freeman, Chairman of the Board of KHC and an officer of each of the Wholly Owned Subsidiaries advised Locke Purnell that it was not authorized to take any actions on behalf of KHC or the Wholly Owned Subsidiaries without the prior authorization of Mr. Freeman. The current management of KHC and the other KHC Appellants did not authorize Locke Purnell either to file any briefs or other papers in the instant appeal of the Confirmed Plan, or to continue to pursue this Appeal.

22. On May 18, 1987, the Boards of Directors of each of the KHC Appellants held board meetings to consider, among other things, the propriety of the continued prosecution of the KHC Appeal before this Court. As a result of these deliberations, the Boards of Directors of each of the KHC Appellants determined that it was not in the best interests of the respective corporations or their various shareholders and creditors to continue to prosecute this appeal. Accordingly, Jones Day was directed to seek a dismissal of the appeals. In addition, the boards of directors determined to waive rights under 28 U.S.C. § 455 to the extent permitted by applicable law.

OTHER SIGNIFICANT EVENTS

23. On August 25, 1987, upon the joint motion of the KHC subsidiaries and certain bank creditors, the Bankruptcy Court dismissed, without prejudice, involuntary petitions filed under Chapter 11 of the Bankruptcy Code against the following subsidiaries of KHC:

Cummins Sales and Service, Inc.
Frigette Corporation
Globe Machinery & Supply Company
Harrisburg, Inc.
Kendavis Industrial Supply Co.
Mechanical Rubber Products Corporation
Miami-Dickerson Steel Company
Midco Equipment Co.
Moore & Sons, Inc.
Rig-A-Lite Company, Inc.
Sligo, Inc.
State Pipe and Supply Co.

Thus, of the 13 involuntary petitions which were filed in May 1985 and which remained pending on the Effective Date, only that against Unit Rig & Equipment Co. remains pending as of the date hereof.

24. In connection with the dismissal of involuntary debtors described in paragraph 23 above, each such debtor undertook to pay all undisputed, liquidated pre-petition claims in full. As of September 1, 1987, payment of an aggregate of approximately $7 million has been made to approximately 2,000 holders of such claims.

25. On August 19, 1987, KHC caused to be filed a motion to dismiss the Chapter 11 case which is pending against Geodril Inc., a wholly owned subsidiary. Such motion is scheduled to be heard by the Bankruptcy Court on October 1, 1987.

26. Since the Effective Date, new management of KHC and/or its subsidiaries have undertaken a number of activities concerning the disposition of significant assets including:

(a) Execution of a contract to sell certain real property of Unit Rig & Equipment Co. for a purchase price of $1.3 million.

(b) Execution of a letter of intent and subsequent contract negotiations for the sale of certain of the assets of the Mid-Continent Division of KECO Limited for an estimated purchase price of approximately $3 million.

(c) Negotiation of a contract for the sale of certain of the assets of Unit Rig & Equipment Co. and the Unit Rig Division of KECO Limited for an estimated purchase price of approximately $26 million.

(d) Solicitation and receipt of bids, and subsequent contract negotiations, for the purchase of substantially all of the assets of Beta Development Co. for a purchase price substantially in excess of $20 million.

In addition, negotiations and solicitations are being actively pursued for the disposition of certain other assets of KHC and/or its subsidiaries.

27. Plans of reorganization of Mid-Continent Supply Co. and for Loffland Brothers Company and its subsidiaries, Loffland Brothers Eastern Hemisphere Inc. and Loffland Brothers (Singapore) Pte. Ltd are currently being developed by management of such companies. In that connection, Loffland Brothers Company has filed objections or motions to determine claims in respect of approximately 1,450 claims aggregating approximately $10 million, and Mid-Continent Supply Company has filed an objection to the claim of its largest trade creditor for in excess of $10 million. In addition, claims of in excess of $30 million in each of the cases involving Geodril Inc., Mid-Continent Supply Co., Loffland Brothers Eastern Hemisphere, Inc. and Loffland Brothers (Singapore) Pte. Ltd. filed

by KHC's insurance carriers have been withdrawn conditioned upon affirmance of the Confirmed Plan by this Court.

28. Through July 1987, the KHC Appellants have incurred and paid on a current basis in excess of $20 million in professional fees in connection with the bankruptcy cases. Certain of such fees have been paid on an interim basis and remain in dispute.

Further affiant sayeth naught.

/s/ David E. Hawthorne

DAVID E. HAWTHORNE

SWORN TO BEFORE ME and subscribed in my presence this 9th day of September, 1987.

/s/ Janet E. Prachyl

Notary Public in and
for the State of Texas

My Commission Expires:

12/11/90

CERTIFICATE OF SERVICE

I, Brett A. Ringle, counsel of record for Respondent Kendavis Holding Company and a member of the Bar of the Supreme Court of the United States, hereby certify that I have served three copies of Respondent Kendavis Holding Company's Brief in Opposition to Petition for Writ of Certiorari and the Joint Appendix to Briefs in Opposition of Respondents Kendavis Holding Company and the Official Unsecured Creditors' Committees on all parties required to be served, by depositing three copies of each in the United States mail, on this 20th day of December, 1987, with first class postage prepaid, addressed to the listed counsel of record at the addresses indicated.

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Supreme Court, U.S.
FILED
DEC 21 1987
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CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

In re KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K. W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A. T. DAVIS, A. T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A. T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T. C. DAVIS, II, T. C. DAVIS, II TRUST, T. C. DAVIS, II TRUST "A", T. C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION, AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T. C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC. AND LOFFLAND BROTHERS COMPANY, KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, THE BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.,

Respondents

RESPONDENT OFFICIAL UNSECURED CREDITORS' COMMITTEES' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTIONS PRESENTED

On November 24, 1986, a United States bankruptcy judge entered an order confirming a plan of reorganization for two corporate debtors proposed by the official unsecured creditors' committees under chapter 11 of title 11 of the United States Code. Four months later and while appeals were pending in the United States district court, the bankruptcy judge disclosed that he had the night before discovered, for the first time, that J. P. Morgan & Co., Inc., a company in which he held stock, owned Morgan Guaranty Trust Company of New York, one of the creditors in the Kendavis related bankruptcy cases over which the judge was then presiding. The bankruptcy judge immediately recused himself pursuant to 28 U.S.C. § 455(b)(4). The district court affirmed the orders of the bankruptcy judge and dismissed the appeal of the respondent committees' plan of reorganization. Thereafter, Petitioners filed a motion to vacate the confirmation order based on the recusal of the bankruptcy judge. The district court denied Petitioners' motion to vacate, concluding that the bankruptcy judge had fully complied with the provisions of § 455. The United States Court of Appeals for the Fifth Circuit affirmed the orders of the bankruptcy court and district court below.

The questions presented are:

1. Whether the requirements of 28 U.S.C. § 455(b)(4) are satisfied when a bankruptcy judge voluntarily recuses himself immediately upon learning that he holds a financial interest in the corporate parent of a creditor in a bankruptcy proceeding pending before him.

2. Whether a bankruptcy judge's impartiality can reasonably be questioned within the meaning of 28 U.S.C. § 455(a) when he voluntarily recuses himself immediately upon acquiring actual knowledge of his financial interest in the corporate parent of a creditor in a bankruptcy proceeding pending before him.

3. Whether Petitioners, who lack standing to raise any other issue on appeal, nonetheless have standing to petition this Court for a writ of certiorari to review confirmation orders based on the disqualification of a bankruptcy judge under 11 U.S.C. § 455.

4. Whether a confirmation order that has been substantially consummated renders the appeal of such order moot.

PARTIES TO PROCEEDING BELOW

In addition to the parties named in the caption of this case, the following were made parties to the proceeding in the Fifth Circuit:

The Bank of New York
The Chase Manhattan Bank, N.A.
CS&S Liquidating Co. (formerly, Cummins Sales & Service, Inc.)
Consolidated Asset Management as Administrator for Federal Deposit Insurance Corporation, in its corporate capacity (formerly, First National Bank & Trust Company of Oklahoma City)
Credit Commercial De France, New York Branch
Den Norske Creditbank
Development Bank of Singapore Limited
First City National Bank of Fort Worth
First City National Bank of Houston
First Interstate Bank of California
First RepublicBank Dallas, N.A. (formerly, InterFirst Bank Dallas, N.A.)
First RepublicBank Fort Worth, N.A. (formerly, InterFirst Bank Fort Worth, N.A.)
Frigette Corporation
Geodril, Inc.
Globe Machinery and Supply Company
Harrisburg, Inc.
Hydril Company
Irving Trust Company
Kendavis Industrial Supply Co.
Loffland Brothers Company
Loffland Brothers Eastern Hemisphere, Inc.
Loffland Brothers (Singapore) Pte., Ltd.
Mechanical Rubber Products Corporation
Miami-Dickerson Steel Company
Midco Equipment Co.
Mid-Continent Supply Co.
Moore & Sons, Inc.
Morgan Guaranty Trust Company of New York
The National Commercial Bank of Saudi Arabia
Nippon Kokan Kabushiki Kaisha
Rig-A-Lite Company, Inc.
Security Pacific National Bank
Sligo, Inc.
State Pipe & Supply Co.
Texas American Bank-Fort Worth, N.A.
Unit Rig & Equipment Co.

Further, pursuant to request of the Clerk of the United States Court of Appeals for the Fifth Circuit, the undersigned previously submitted a list of all of the pre-petition creditors in the Kendavis related cases. There were approximately 10,835 creditors on the list that was furnished to the Fifth Circuit. If this Court so directs, the undersigned will submit an identical list of creditors to this Court.

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No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

K. W. DAVIS, JR., et al.,

Petitioners

v.

OFFICIAL UNSECURED CREDITORS' COMMITTEES, et al.,

Respondents

RESPONDENT OFFICIAL UNSECURED CREDITORS' COMMITTEES' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondent Official Unsecured Creditors' Committees of Kendavis Holding Company ("KHC"), Kendavis Industries International, Inc. ("KIII") and Loffland Brothers Company ("Loffland") (the "Respondent Committees")[1] respectfully pray that the Court deny the petition for writ of certiorari.

[1] The members of the KHC creditors' committee are Security Pacific National Bank, The Bank of Nova Scotia, Morgan Guaranty Trust Company of New York, Continental Illinois National Bank and Trust Company of Chicago as Administrator for Federal Deposit Insurance Corporation, The Bank of New York, MBank Houston, N.A., First Interstate Bank of California, Irving Trust Company, The Chase Manhattan Bank, N.A., First City National Bank of Houston and Credit Commercial de France, New York Branch. Membership of the KIII creditors' committee is identical to the membership of the KHC creditors' committee, except that Consolidated Asset Management Company as Administrator for Federal Deposit Insurance Corporation, in its Corporate Capacity (formerly, First National Bank & Trust Company of Oklahoma City) is a member of the KIII and Loffland committees only. Membership of the Loffland creditors' committee is identical to the membership of the KIII creditors' committee, except that Hydril Company is a member of the Loffland creditors' committee only.

REASONS FOR NOT GRANTING THE WRIT

1. The decision of the United States Court of Appeals for the Fifth Circuit is in accordance with legal precedent from other circuits.

2. The decision of the United States Court of Appeals for the Fifth Circuit presents no novel legal analysis warranting this Court's review.

3. The United States Court of Appeals for the Fifth Circuit limited its decision to the specific facts of this case.

4. The district court and the United States Court of Appeals for the Fifth Circuit correctly found that the bankruptcy judge complied with the requirements of 28 U.S.C. § 455(b)(4) when he voluntarily recused himself immediately upon acquiring actual knowledge of his indirect financial interest in one of the creditors in a bankruptcy proceeding pending before him.

5. The district court and the United States Court of Appeals for the Fifth Circuit correctly found that the bankruptcy judge complied with the requirements of 28 U.S.C. § 455(a).

6. The district court correctly found that Petitioners lack standing to appeal, and thus Petitioners lack standing to seek a writ of certiorari.

7. The Respondent Committees' plan of reorganization has been substantially consummated and Petitioners' appeal is therefore moot.

STATEMENT OF THE CASE

This petition relates to orders of the United States Bankruptcy Court for the Northern District of Texas, the Honorable Robert C. McGuire presiding (the "Bankruptcy Court"), confirming the Respondent Committees' Modified Joint Plan of Reorganization (the "Committees' Plan") as to KIII and KHC, and denying confirmation of the Debtors' Third Amended Joint Plan of Reorganization ("Debtors' Plan").[2] On March 26, 1987, those orders were affirmed by the United States District Court for the Northern District of Texas, Dallas Division, the Honorable A. Joe Fish presiding (the "District Court"). R.App.-10. On September 24, 1987, the United States Court of Appeals for the Fifth Circuit (the "Fifth Circuit") affirmed the District Court decision. Pet.App.-6.

The chapter 11 cases of KIII and KHC commenced on February 21, 1985 when eight unsecured institutional creditors that were owed in excess of $440 million, filed involuntary petitions for relief.[3] KIII and KHC consented to the filings and orders for relief were entered on March 19, 1985. KHC and KIII were insolvent at the commencement of their cases, and their insolvency throughout the proceedings was not disputed by any party during the course of the confirmation hearings or on appeal of either the Debtors' Plan or the Committees' Plan. At no time during the course of the hearings on the Committees' Plan did Petitioners ever file an objection to the Committees' Plan or appear in opposition to its confirmation.

Hearings on the competing Debtors' Plan and the Committees' Plan lasted from May 7, 1986 until June 24, 1986, and

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[2] The proponents of the Debtors' Plan were KHC, KIII, Loffland, Loffland Brothers Eastern Hemisphere, Inc., Loffland Brothers (Singapore) Pte., Ltd., Mid-Continent Supply Co. and Geodril, Inc. (collectively, the "Debtors"). At the time that the Debtors' Plan was proposed, the Petitioners managed and controlled each of the Debtors.

[3] KIII and KHC owed approximately $500 million in aggregate institutional debt. Noninstitutional debt was less than one percent (1%) of KIII's and KHC's debt.

from June 25, 1986 until November 12, 1986, respectively. The Bankruptcy Court's confirmation of the Committees' Plan and denial of the Debtors' Plan was a carefully studied, well informed decision by Judge McGuire, based upon a voluminous record.

On March 22, 1987, approximately four months after entry of the order confirming the Committees' Plan, Judge McGuire learned, for the first time, that a company in which he held stock, J.P. Morgan & Co., Inc. ("J.P. Morgan"), is the parent company of one of the bank creditors in these cases, Morgan Guaranty Trust Company of New York ("Morgan Guaranty"). On March 23, 1987, Judge McGuire advised the parties' counsel by telephone conference call that while reading *The Value Line Investment Survey ("Value Line")* the night before, he discovered for the very first time that J.P. Morgan owned Morgan Guaranty. Pet.App.-19. During this same conference, Judge McGuire stated that in response to an inquiry he made to his stock broker early in the proceedings, he recalled being informed that J.P. Morgan and Morgan Guaranty were unconnected entities. *Id.* According to Judge McGuire, the late discovery came "out of the blue." Pet.App.-20. Judge McGuire's holding is a miniscule percentage of the outstanding stock of J.P. Morgan, and the amounts owed to Morgan Guaranty in these cases are a similarly tiny fraction of that bank's assets. Thus, these cases do not have any impact upon Judge McGuire's finances. Nonetheless, as required by 28 U.S.C. § 455, Judge McGuire immediately advised the parties of his holding, and recused himself from hearing the case without taking any further action in the proceedings. Pet.App.-7, 14, 18.

On March 26, 1987, the District Court entered various orders and judgments affirming the Bankruptcy Court orders. The District Court concluded, in part, that Petitioners herein "are not aggrieved persons and have no standing to appeal." R.App.-4. On March 31, 1987, Petitioners filed in the District

Court motions pursuant to Fed. R. Civ. P. 60(b)(4) and (6) to vacate the confirmation orders, based upon the circumstances of Judge McGuire's recusal. In these motions, there were no allegations of actual bias, partiality or impropriety on the part of Judge McGuire, and no affidavits of any kind to that effect were filed. On April 10, 1987, the District Court denied the motions to vacate on their merits.[4] Pet.App.-11. Although again concluding that Petitioners arguably lacked standing to seek a retrospective recusal, the District Court also ruled on the merits that there was no violation of 28 U.S.C. § 455(b)(4), no "constructive knowledge" on the part of Judge McGuire and no basis for reasonably doubting the bankruptcy judge's impartiality within the meaning of 28 U.S.C. § 455(a). *Id.* The District Court also stated that no due process violation resulted from the unknown, insubstantial interest. *Id.*

Upon review by the Fifth Circuit, the court of appeals held that all but one of the many points of error asserted by Petitioners were "frivolous." Pet.App.-7. On the remaining issue of judicial disqualification, the court of appeals held that under the specific circumstances of this case, the District Court "was entitled to accept the bankruptcy judge's statement of his lack of knowledge that the corporation in which he held stock was the corporate parent of a creditor of the . . . debtor and might be affected by the outcome of the proceeding." Pet.App.-7. The Fifth Circuit found that the record did not justify questioning Judge McGuire's assurance. *Id.* Furthermore, the Fifth Circuit found "it clear that Judge McGuire's impartiality could not reasonably be questioned." *Id.* Thus, both the District Court and the Fifth Circuit properly concluded that based upon the specific facts of this case, Judge McGuire had fully complied with the provisions of 28 U.S.C. § 455. Because the Fifth Circuit found that neither § 455(b)(4) nor 455(a)

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[4] The District Court deemed Petitioners' motion to vacate to have been brought under Fed. R. Civ. P. 59, citing *Harcon Barge Co., Inc. v. D & G Boat Rentals, Inc.*, 784 F.2d 665, 667 (5th Cir.) (en banc), *cert. denied*, 107 S. Ct. 398 (1986). Pet.App.-12 n.1.

was violated, the court of appeals was not required to determine whether a violation of § 455 requires only prospective recusal or whether, and under what circumstances, retroactive relief is appropriate.

Under the self executing terms of the Committees' Plan, its "effective date" occurred on April 16, 1987. Petitioners failed to seek a stay of the implementation of the Committees' Plan. The District Court denied two separate stay motions that were filed only by the Debtors and other corporate appellants, and the Fifth Circuit denied an emergency stay motion, again, filed only by the Debtors and other corporate appellants. Consequently, on April 16, 1987, pursuant to the terms of the Committees' Plan, all of the prior capital stock of KHC held by Petitioners was cancelled. KIII was statutorily merged into KHC, a new board of directors and chief executive officer were installed, and new capital stock was issued to the Class 7 creditors. New boards of directors were subsequently elected for all of the KHC subsidiaries. *See* R.App.-12 for Amended Affidavit of David E. Hawthorne.

All of the creditors in Classes 1 through 6 under the Committees' Plan have either been paid in full or had their rights reinstated, thereby representing full satisfaction of those claims. Further, KHC distributed approximately $40 million in available cash to the Class 7 creditors and made their first interest payment, aggregating approximately $4.7 million, in respect of the notes issued to Class 7 creditors under the Committees' Plan. R.App.-16, 17. The Committees' Plan, thus, has been substantially consummated.

SUMMARY OF THE ARGUMENT

Judge McGuire complied with the plain terms of 28 U.S.C. § 455 when he immediately recused himself after learning that J.P. Morgan, a company in which he owned stock, was the corporate parent of Morgan Guaranty, one of the creditors in the Kendavis related bankruptcy proceedings pending before him.[5] The Fifth Circuit correctly held that when the facts of this case are applied to "well-settled principles of law,"[6] neither § 455(a) nor (b)(4) were violated. Section 455(b)(4) requires actual knowledge of a financial interest on the part of a judge. As found by both the District Court and the Fifth Circuit, this section is therefore inapplicable to Judge McGuire's prior rulings due to his total lack of knowledge of his financial interest in a creditor before him. Further, because of Judge McGuire's lack of knowledge, the Fifth Circuit correctly held that Judge McGuire's impartiality could not reasonably be questioned and therefore § 455(a) likewise requires no remedy under the facts of this case. The Fifth Circuit also properly found that the District Court did not abuse its discretion in denying discovery of Judge McGuire due to the absence of any allegations or affidavits of *actual* impropriety, bias or unfair treatment on the part of Judge McGuire. Because of the absence of such allegations or affidavits, the Fifth Circuit correctly rejected Petitioners' due process claim.

In addition, by failing to either file an objection to the Committees' Plan or otherwise appear in opposition to its

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[5] While the number of creditors in the KHC and KIII bankruptcy cases were relatively modest, the Kendavis related bankruptcy proceedings at the time of the confirmation hearings involved seven separate chapter 11 proceedings and thirteen separate involuntary bankruptcy proceedings aggregating in excess of 10,800 creditors.

[6] The Fifth Circuit's *per curiam* opinion was issued pursuant to its local rule 47.5 which provides: "The publication of opinions that have no precedential value and merely decide particular cases on the basis of well-settled principles of law imposes needless expense on the public and burdens on the legal profession." The Fifth Circuit opinion was not published.

confirmation, Petitioners have not preserved their right to appeal. Further, Petitioners are not "aggrieved" by the orders confirming the Committees' Plan since Petitioners' interests in an insolvent KHC are without value. R.App.-4. Accordingly, Petitioners have no direct pecuniary interest in these appeals and therefore lack standing to appeal.

Finally, the Committees' Plan has now been substantially consummated. Ownership of the debtor corporations has been transferred from the Petitioners, who are the former shareholders, to the creditors. All creditors with allowed claims, other than Class 7 creditors, have been paid in full. Reservations of cash have been made for creditors with contested claims so that if and when those claims are allowed, they will also be paid in full. Thus, any appeal of the Committees' Plan is now moot.

ARGUMENT

POINT I

JUDGE MCGUIRE RECUSED HIMSELF IN COMPLIANCE WITH 28 U.S.C. § 455 AND HIS ORDERS ARE THEREFORE VALID

Much of Petitioner's argument is dedicated to the notion that Judge McGuire should have been disqualified, prospectively. But the issue of whether § 455 required Judge McGuire's prospective recusal is not germane, since, as discussed below, Judge McGuire correctly recused himself. Rather, the question is whether almost three years and many million dollars of reorganization toil should be held for naught based merely on an alleged appearance of partiality when the courts below have each concluded that Judge McGuire clearly fulfilled the requirements of § 455, and where the Fifth Circuit has held that the Petitioners' substantive claims on appeal were frivolous.

a. **28 U.S.C. § 455(b)(4) does not require disqualification of a bankruptcy judge prior to the judge acquiring actual knowledge of his financial interest in a creditor in the proceeding.**

Section 455(b)(4) provides that a judge shall disqualify himself when "he knows that he . . . has a financial interest . . . in a party to the proceeding." 28 U.S.C. § 455(b)(4). This is a two part test applied uniformly among the circuits that requires "knowledge" of both a "financial interest" and the fact that the financial interest is "in a party to the proceeding." *See Davis v. Xerox*, 811 F.2d 1293, 1295 (9th Cir.), *cert. denied*, 56 U.S.L.W. 3383 (U.S. Nov. 30, 1987); *Hodosh v. Block Drug Co., Inc.*, 790 F.2d 880, 881 (Fed. Cir.), *cert. denied*, 107 S. Ct. 106 (1986); *Union Carbide Corp. v. U.S. Cutting Service, Inc.*, 782 F.2d 710, 714 (7th Cir. 1986); *NEC Corp. v. Intel Corp.*, 654 F. Supp. 1256, 1257-58 (N.D. Cal. 1987), *appeal docketed*, No. 87-7126 (9th Cir. Mar. 30, 1987); *Catherines v. Copytele, Inc.*, 608 F. Supp. 1031, 1032 (E.D.N.Y. 1985); *In re Cement and Concrete Antitrust Litigation*, 515 F. Supp. 1076, 1081 (D. Ariz. 1981), *appeal dism'd*, 673 F.2d 1020 (9th Cir. 1982), *mand. denied*, 688 F.2d 1297 (9th Cir. 1982), *aff'd for want of a quorum*, 459 U.S. 1191 (1983); *see also Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796, 802 (5th Cir. 1986), *cert. granted*, 107 S. Ct. 1368 (1987) (argued Dec. 9, 1987) (No. 86-957). The mere existence of a financial interest is not in and of itself disqualifying because a judge who is unaware that he has a financial interest in a party to a proceeding before him has no incentive to favor the party. *Union Carbide v. U.S. Cutting Service*, 782 F.2d at 714 ("Before [the judge] discovered she had a financial interest, she could have had no incentive to favor the plaintiffs; when she knew she had an interest, she made no rulings in the case . . .").

Generally, a judge who learns that he has a financial or other interest in a case is only required to recuse himself from future proceedings, following the discovery of such interest. *See Health Services*, 796 F.2d at 801; *In re Cement and*

Concrete Antitrust Litigation, 515 F. Supp. at 1081-82; 13A C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure*, § 3546 at 600 n.13 (1984). Only when the judge has had actual prior knowledge of an interest, and nevertheless proceeds to hear the case will his rulings be vacated under 455(b)(4).[7]

Petitioners' argument for the use of a "constructive knowledge" or "should have known" test in application of § 455(b)(4) is contrary to the plain reading of § 455(b)(4), the well-established principles of law uniformly followed among the circuits and the statute's legislative history.[8] In cases decided to date, no court has ever applied § 455(b)(4) to vacate orders of a judge that were issued before the judge actually learned of the relevant financial interest. *See Davis v. Xerox*, 811 F.2d at 1296; *Hodash v. Block Drugs*, 790 F.2d at 881; *Union Carbide v. U.S. Cutting Service*, 782 F.2d at 715; *NEC v. Intel*, 654 F. Supp. at 1259; *Catherines v. Copytele*, 608 F. Supp. at 1032; *In re Cement and Concrete Antitrust Litigation*, 515 F. Supp. at 1081.

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[7] *Compare Potaschnick v. Port City Construction Co.*, 609 F.2d 1101 (5th Cir.) *cert. denied*, 499 U.S. 820 (1980), which involved actual knowledge as required under 455(b)(5)(iii) *with Mixon v. United States*, 620 F.2d 486 (5th Cir. 1980), which involved a *per se* violation of § 455(b)(3) where knowledge is *not* a statutory element. *See infra* at 12 n.12.

[8] Congress rejected the conclusive "presumption" of knowledge theory suggested by Petitioners when it failed to adopt Senate Bill 1886 introduced in 1971 by Senator Birch Bayh which provided that a judge shall disqualify himself "in *any case* in which he has an interest." Congress instead enacted Senate Bill 1064 introduced in 1973 by Senator Quentin N. Burdick which provided that a judge shall disqualify himself when "he *knows* that he, individually or as in fiduciary . . . has a financial interest . . . in a party to the proceeding." *Judicial Disqualification: Hearings on S. 1064 Before the Subcommittee on Improvements in Judicial Machinery of the Senate Committee on the Judiciary*, 93rd Cong. 1st Sess. 1 (1973) (emphasis added) [hereinafter "*Senate Hearings*"] (Hearings held on July 14, 1971 and May 17, 1973 were reported in a single document with consecutive pagination). *Compare* S. 1886, Senate Hearings at 6-8 *with* S. 1064, Senate Hearings at 130-133. Senate Bill 1064 was supported by the American Bar Association and modeled after Canon 3C(1) of the Code of Judicial Conduct of the American Bar Association.

Accordingly, the orders of a disqualified judge entered before acquiring actual knowledge of an interest in a party remain valid orders. Judge McGuire, who did not have actual prior knowledge, has thus fulfilled the requirements of § 455(b)(4) by his prospective recusal, commencing when he first learned of the interest.[9] The Fifth Circuit correctly found that the District Court was entitled to accept Judge McGuire's statement of his lack of knowledge, and that the record does not justify questioning Judge McGuire's assurance.[10] Pet.App.-7.

Section 455(c) requires that a judge "inform himself about his personal and fiduciary financial interests." In these cases, Judge McGuire satisfied this section by inquiring early in the proceedings whether the interest he held in J.P. Morgan was connected to a bank creditor in these cases. He recalled being advised that there was no connection, and accordingly believed that there was none. Judge McGuire cannot be faulted for relying upon his broker. *Cf. Catherines v. Copytele, Inc.*, 608 F. Supp. at 1032 (trial judge looked first to the advise of his broker). As the District Court ruled, Judge McGuire thus had no reason for making further review of documents to determine whether any such relationship existed. Pet.App.-15.

The gravamen of Petitioners' position regarding § 455(c) and § 455(b)(4) is that, for purposes of determining whether *past* rulings should be undone, it is not enough for a judge to

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[9] There is support for the proposition that Judge McGuire could have continued hearing this case if he disposed of his stock upon acquiring actual knowledge of his interest in a creditor. *See The Advisory Committee on Codes of Conduct of the Judicial Conference of the United States (Oct. 15, 1981), Advisory Opinion* 69 [hereinafter *"Advisory Opinion"*] (concluding that disposing of disqualifying interest when it surfaces after the judge has been sitting on the case for some time would remove the disqualification and permit the judge to continue to sit). *Advisory Opinion* 69 was relied upon by *Union Carbide v. U.S. Cutting Service*, 782 F.2d at 715.

[10] All determinations relating to disqualification are reviewed under the abuse of discretion standard. *See, e.g., In re Placid Oil Co.*, 802 F.2d 783, 786 (5th Cir. 1986); *In re City of Houston*, 745 F.2d 925, 927 (5th Cir. 1984); *United States v. Gregory*, 656 F.2d 1132, 1136 (5th Cir. 1981).

make a reasonable inquiry of his financial interests; rather, the judge must successfully uncover every possible conflict, even in a case which involves thousands of creditors, many owned by holding companies or conglomerates.[11] According to Petitioners, if the already busy bankruptcy judge fails to actually uncover a latent conflict, the losing party should always have a new trial, even when the interest is not substantial. A rule along those lines would be unwieldy, inefficient and unfair, particularly in large banktuptcy cases. Indeed, such a rule would emasculate the "knowledge" requirement contained in § 455(b)(4).[12] In essence, Petitioners' reading of § 455(c) and § 455(b)(4) requires the judge to do the impossible — to recuse himself on the basis of facts that he does not know.

Further, Petitioners, who never reviewed Judge McGuire's financial disclosurers themselves, are in no position to question the scope or quality of his review. Because the ownership of J.P. Morgan stock was disclosed in the judge's financial reports of record and available to the public, why should Petitioners not be charged with this knowledge? And if "constructive knowledge" should be imputed to Judge McGuire because of securities filings, proxy statements or previously unobserved

[11] Recognizing that judges might unwittingly have a financial interest in a party to a proceeding before them, Congress concluded that in amending the statute, § 455 must have some reasonable standard of "knowledge." *See, e.g.*, colloquy of Senator Burdick and Senator Gurney during the testimony of John P. Frank. *Senate Hearings* at 38.

[12] It should be presumed that Congress acted intentionally and purposefully when it included the knowledge requirement in § 455(b)(4). *See Reiter v. Sonotone Corp.*, 442 U.S. 320, 339 (1979) ("In construing a statute [courts] are obliged to give effect, if possible, to every word Congress used"); *United States v. Menasche*, 348 U.S. 528, 538-539 (1955) ("It is our duty 'to give effect, if possible, to every clause and word of a statute,' . . . rather than to emasculate an entire section [citations omitted]."); *see also Russello v. United States*, 464 U.S. 16, 23 (1983) ("[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acted intentionally and purposely in the disparate inclusion or exclusion"). *See supra* at 10 n.7.

portions of *Value Line*, why would it not also be imputed to Petitioners. And, if so, Petitioners have arguably long since waived any complaint. *Cf. Delesdernier v. Porterie*, 666 F.2d 116, 121-23 (5th Cir.), *cert. denied*, 459 U.S. 839 (1982); *see also United States v. Murphy*, 768 F.2d 1518, 1540-41 (7th Cir. 1985), *cert. denied*, 475 U.S. 1012 (1986).

b. **A bankruptcy judge's impartiality cannot reasonably be questioned within the meaning of 28 U.S.C. § 455(a) when he voluntarily recuses himself immediately upon acquiring actual knowledge of his financial interest in a creditor in the proceeding.**

Section 455(a) provides that a judge "shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned." 28 U.S.C. § 455(a). Rather than explicitly requiring knowledge, § 455(a) establishes an objective test that looks to whether "the reasonable man, were he to know all the circumstances would harbor doubts about the judge's impartiality." *Potaschnick*, 609 F.2d at 1111; *see e.g., New York Housing Development Corp. v. Hart*, 796 F.2d 976, 980 (7th Cir. 1986); *United States v. Greenough*, 782 F.2d 1556, 1558 (11th Cir. 1986); *Rice v. McKenzie*, 581 F.2d 1114, 1116 (4th Cir. 1978). The District Court found below that a reasonable person would not harbor doubts about Judge McGuire's impartiality due to his prior lack of knowledge regarding the connection between Morgan Guaranty and J. P. Morgan. Pet.App.-15. The Fifth Circuit found it clear that Judge McGuire's impartiality could not reasonably be questioned. Pet.App.-7. Any "doubt" to the contrary would only be speculation, which will not support recusal. *Kinnear-Weed Corporation v. Humble Oil and Refining Co.*, 441 F.2d 631, 634-35 (5th Cir. 1971) *("Kinnear II"); see also Health Services*, 796 F.2d at 803; *Margoles v. Johns*, 660 F.2d 291, 298 (7th Cir.), *cert. denied*, 455 U.S. 909 (1982). To support reversal in these cases, a reasonable person knowing "all the circumstances" would have to speculate not only that Judge McGuire was not telling the truth in stating that he had no actual prior

knowledge of his financial interest after disclosing his discovery of such interest, but also that this reasonable person somehow knew more about Judge McGuire's knowledge than both the District Court and Fifth Circuit who reviewed the record and found no merit in Petitioners' claims.

Further, where as discussed above, only § 455(a) can have any application, the notion of substantial interest, unlike § 455(b)(4), is relevant in determining that Judge McGuire's insubstantial interest in J.P. Morgan would not cause a reasonable person knowing all the circumstances to question his impartiality. Here, Judge McGuire's 808 shares of J.P. Morgan constitute, according to affidavits submitted to the District Court, approximately .00023% of that company's outstanding capital stock. Pet.App.-16. The $27,000,000 claimed by Morgan Guaranty against KIII and KHC is approximately .036% of the reported assets of that company. The recoveries in these cases to bank claimants were estimated in the confirmation hearings to be in the range of 65%, realized over several years. These fractions show that a holder of such a minor interest, even with prior knowledge, could not have reasonably expected a noticeable financial enhancement in this case. Even in the unlikely scenario in which the subsidiary bank were to receive *no* recoveries in the case, Judge McGuire's holding could not be impacted even by two cents. The interest is thus so insubstantial, under any approach, that a reasonable person knowing all the circumstances would not question Judge McGuire's impartiality. Accordingly, over two years of hearings and rulings should not be vacated.

c. **28 U.S.C. § 455 does not contemplate vacating a judgment on appeal where the bankruptcy judge's rulings were made prior to his acquiring actual knowledge of his financial interest in a creditor in the proceeding.**

The Ninth Circuit, relying in part on *Health Services*, reasoned in *Davis v. Xerox*, 811 F.2d at 1296:

> The case is different, however, when the statute is not to be applied prospectively, but to be applied retro-

> spectively to rulings the judge has already made. In such retrospective applications we find wisdom in the observation of the Fifth Circuit interpreting Section 455(a): 'Because of the harsh consequences that can result, knowledge of fact should not lightly be imputed to a judge [*Health Services*, 796 F.2d at 803].' We are unwilling to presume that because the judge once knew, he could not have forgotten. The right course under § 455(b) as under § 455(a) is to proceed on a case by case basis, determining the existence of disqualifying knowledge at the time the judge sat, in the way that a state of mind is normally determined, from inspection of all the circumstances. If a reasonable person would conclude from all the circumstances that the judge did not have knowledge at the time he sat, his rulings stand. . .

In that case, the Ninth Circuit upheld the prior rulings of the trial court, reasoning on the facts of that case that a reasonable person would not harbor doubts about the trial judge's claim that he had forgotten about his financial interest. The views of the Seventh Circuit and Federal Circuit on the effect of recusal on prior rulings are expressed in *United States v. Murphy*, 768 F.2d 1518 (7th Cir. 1985), *cert. denied*, 475 U.S. 1012 (1986) (no judicial acts taken before a § 455(a) motion may be set aside); *New York Housing Development Corp. v. Hart*, 796 F.2d at 979; *Falconer v. Meehan*, 804 F.2d 72, 78 (7th Cir. 1986) and *Hodosh v. Block Drug Co.*, 790 F.2d at 881 (Fed. Cir. 1980) (refusing to vacate court of appeals decision where one of the panel judges did not know that his spouse owned stock in the parent company of a party to the appeal).

In *Health Services*, the Fifth Circuit granted retrospective disqualification under § 455(a), based upon a determination that the original trial judge had "constructive knowledge" of certain crucial facts. The District Court in these cases concluded, however, that the facts of *Health Services* are a "far cry" from the specific facts of the instant cases. Pet.App.-15. The two cases can be distinguished on a number of grounds.

First, the judge in *Health Services* knew of his interest very soon before the trial but forgot about his interest. Judge McGuire, on the other hand, never knew of the connection between Morgan Guaranty and J.P. Morgan until the night before he fully disclosed all the facts. Second, the judge in *Health Services* made no investigation of his interest at any time during that case, while Judge McGuire made a proper inquiry to his broker regarding the connection between Morgan Guaranty and J.P. Morgan but unwittingly operated under honestly mistaken advice. Third, the outcome of *Health Services* was found to be material to that judge's interest in the case, but as demonstrated above, the outcome of these cases could have no financial impact on Judge McGuire. Fourth, the judge in *Health Services* apparently did not make a timely disclosure to the parties, and later was unclear as to when actual knowledge had been obtained. Judge McGuire, on the other hand, made an immediate and full disclosure, which specified unequivocally *when* the knowledge was acquired. Fifth, the *Health Services* judge erred in failing to recuse himself, even after reacquiring actual knowledge of his interest. Judge McGuire, on the other hand, took immediate action when he first learned of a possible conflict. Finally, the trial judge in *Health Services* continued to hear substantive contested matters after reacquiring actual knowledge. Conversely, Judge McGuire ceased to hear any further matters on the first occasion of his obtaining actual knowledge. These differences alone would compel an informed "reasonable man" to a different conclusion about Judge McGuire than that reached concerning the *Health Services* judge. The Fifth Circuit found it "clear" that Judge McGuire's impartiality could not be reasonably questioned. Pet.App.-7.[13]

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[13] Other cases requiring retrospective recusal are also readily distinguishable. In *Potaschnick*, 609 F.2d 1101, the court was fully aware of the conflict prior to hearing the case, and advised the parties of the conflict, but proceeded to try the case on the premise of consent. In *Hall v. Small Business Administration*, 695 F.2d 175 (5th Cir. 1983), the magistrate's law clerk had accepted employment with the firm representing one of the parties to a class action lawsuit. The magistrate did not immediately take the law clerk off all work on the case, even though *aware* of the clerk's prospective employment.

As illuminated in *Davis v. Xerox*, 811 F.2d at 1296, the *Health Services* opinion notes that knowledge should *not* lightly be imputed to a judge. The overly broad expansion of the "constructive knowledge" test urged by Petitioners is inappropriate. Moreover, "[w]here a reasonable man would only speculate that a judge might have actual knowledge of the facts, constructive knowledge does not exist." *Health Services*, 796 F.2d at 803. The Respondent Committees submit that the *Murphy* rule denying retrospective relief absent actual impropriety is the correct analysis of § 455(a). But as discussed above, under the specific facts of this case, the Fifth Circuit's ruling is not inconsistent with its own prior ruling in *Health Services* or the rulings of any other court. Accordingly, this case does not merit this Court's review.[14]

d. The confirmation related orders satisfy due process and are therefore not void.

"A judgment is not void merely because it is erroneous. It is void only if the court that rendered it lacked jurisdiction . . . or or if it acted in a manner inconsistent with due process of law." 11 C. Wright & A. Miller, *Federal Practice & Procedure* § 2862 (1973). Not all questions of judicial qualification, however, involve constitutional validity. *Aetna Life Insurance Co. v. Lavoie*, 475 U.S. 813, 820 (1986) (*citing Tumey v. Ohio*, 273 U.S. 510, 523 (1927)). Due process is violated when a person's liberty or property is subjected to a "judgment of a court the judge of which has a direct, personal, substantial, pecuniary interest in reaching a conclusion against him in his case." 475 U.S. at 821-22 (*citing Tumey*, 273 U.S. at 523). What constitutes a "direct, personal, substantial, pecu-

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[14] Respondent Committees submit that under the specific facts of this case, the circuit courts are in accord that no retrospective application of § 455 is warranted. To the extent there is a conflict between the Seventh and Fifth Circuits concerning when retrospective application of § 455 is appropriate, that conflict will likely be resolved by this Court in *Health Services*, *supra*. That decision, however, is not necessary to the case at bar.

niary interest' has been formulated by this Court to be a situation

> which would offer a possible temptation to the average . . . judge to . . . lead him not to hold the balance nice, clear and true . . .

Ward v. Village of Monroeville, 409 U.S. 57, 60 (1972) (*cited with approval* in *Lavoie, supra* at 822).

In applying the above constitutional standard to the specific facts of this case, it is clear that Judge McGuire's indirect interest in Morgan Guaranty did not constitute a "direct, personal, substantial, pecuniary interest" in the outcome of the Kendavis bankruptcy proceedings. Moreover, the Fifth Circuit in determining that there was no violation of 28 U.S.C. § 455, ruled it is clear that Judge McGuire's impartiality could not reasonably be questioned.

Because Petitioners have failed to establish any violation of § 455, they consequently fail in their efforts to establish a violation of fifth amendment due process. *See United States v. International Business Machines,* 475 F. Supp. 1372, 1390 (S.D.N.Y. 1979), *aff'd,* 618 F.2d 923, 932 n.11 (2d Cir. 1980). "It would be anomalous to hold a claim under the statutes [28 U.S.C. §§ 144, 455] insufficient on its merits could nevertheless satisfy the constitutional standard." *Id.* at 932 n.11. *See also* Pet.App.-16. If a claim of bias and prejudice passes the rigid scrutiny of § 455, it will necessarily pass constitutional muster as well. *International Business Machines,* 475 F. Supp. at 932 n.11.

e. **The District Court did not err in denying discovery of Judge McGuire.**

Petitioners' assertion that they were entitled to discovery, including the deposition of Judge McGuire, constitutes a mere ruse for delay.[15] The vast majority of disqualification cases have

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[15] The Fifth Circuit correctly noted that orders have been entered by the successor bankruptcy judge in these cases and steps have been taken by the successor corporation implementing the Committees' Plan. An evidentiary hearing would only add needless expense and delay the necessary continued implementation of the Committees' Plan. Pet. App.-7.

wisely been determined solely on the strength of statements or letters by the trial court, without any depositions or cross-examination of judges. In *Hunt v. Mobil Oil Corporation*, 654 F. Supp. 1487, 1495-96 (S.D.N.Y. 1987) (*citing Andros Compania Maritime, S.A. v. Marc Rich & Co.*, 579 F.2d 691, 701 (2d Cir. 1978)), a case in which motions to depose a Title 9 arbitrator and to vacate awards were denied, Judge Edward Weinfeld Wrote:

> To invoke the discovery and deposition process in a search for evidence to support the charges would be tantamount to requiring a judge to submit to an oral deposition by a non-prevailing party where the judge had refused to recuse himself on allegations of personal bias under 28 U.S.C. § 455.
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> [T]he Court [Second Circuit] made it clear that the [discovery] procedure should be invoked only under judicial supervision *and 'limited to situations where clear evidence of impropriety has been presented.'* [citing *Andros*]. The instant case clearly is not such a situation; on the contrary, it is an attempt to use, more correctly abuse, the discovery process as a fishing expedition which would needlessly delay the proceeding. *Post-verdict examinations of a judicial or quasi-judicial officer, be he judge, juror, or arbitrator, for the purpose of impeaching his decision are 'inherently suspect, indeed, roundly condemned, in our system of jurisprudence.'*

654 F. Supp. at 1495 n.13 (citations omitted) (emphasis added).

If depositions of judges are to be permitted in any case, "clear evidence of impropriety" should first be demonstrated in order to prevent abuse. In *Ricci v. Key Bancshares of Maine*,

Inc., 111 F.R.D. 369, 373 n.4 (D. Me. 1986), a case in which the request to depose the judge was denied, the court opined:

> [A] motion to recuse is not a mere pleading, a first step towards a possible case. Like any public official, a judge is presumed qualified to act, and an objector must come with a prima facie case, not just a hope of developing one.

The instant case involves no hint or allegation, and certainly no affidavit of prior actual knowledge, or any other *per se* violation or actual impropriety. Even when allegations of actual knowledge or impropriety are advanced however, the attempts by a losing litigant to depose the trial judge should be subject to stringent judicial control and discretion, in order to protect the courts and public against trivial and vexatious litigation.

But, particularly as in these cases where only "constructive knowledge" can even be colorably alleged, the movant should be required at the outset to articulate and substantiate, by affidavit where appropriate, a rational basis for the imputation of "constructive knowledge" before proceeding further. It should be remembered that "Congress did not enact § 455(a) to allow counsel to make a game of the federal judiciary's ethical obligations," and that courts "should seek to preserve the integrity of the statute by discouraging bad faith manipulation of its rights for litigious advantage." *Delesdernier*, 666 F.2d at 121. The record is adequate for a reasonable person to conclude that Petitioners did not meet their threshold of proof necessary to depose Judge McGuire. The Fifth Circuit properly found that the District Court did not abuse its discretion in rejecting the drastic remedy of vacating all of Judge McGuire's

rulings and refusing to set the dangerous precedent of allowing his deposition.[16]

f. **Public policy disfavors a retrospective remedy in these cases.**

Petitioners hope to persuade this Court that public confidence in the judicial system will be enhanced by vacating the orders below because of an imagined appearance of partiality by Judge McGuire.[17] The public interest in judicial purity is not undercut, however, where the judge's financial interest is disclosed by the trial court immediately upon first learning of an interest. Unless substantive, non-speculative contradictions to the reasonable observer are apparent from affidavits or publicly available documents, the public and the judiciary would be ill-served by any process that undoes sound determinations or permits vexatious fishing expeditions to be commenced by a losing litigant against the trial judge.

Further, today's bankruptcy judges hear cases in which there are tens of thousands of creditors. The goals of § 455 are

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[16] A judge's decision to deny recusal motions without formal hearings is subject to the "clear abuse" rule. *United States Fidelity & Guaranty Co. v. Lawrenson*, 34 F.R.D. 121, 123 (D.Md.) *aff'd*, 334 F.2d 464 (4th Cir. 1964), *cert. denied*, 379 U.S. 869 (1964); *Harris v. Illinois-California Express, Inc.*, 687 F.2d 1361, 1374 (10th Cir. 1982); *cf.* Bankruptcy Rule 8011. For application of the clear abuse standard to matters under Fed. R. Civ. P. 59 or 60(b) *see Adams v. Johns-Manville Sales Corp.*, 727 F.2d 533, 539 (5th Cir. 1984); *In re Ta Chi Navigation (Panama) Corp.* 728 F.2d 699, 703 (5th Cir. 1984); *Verret v. Elliot Equipment Corp.*, 734 F.2d 235 (5th Cir. 1984); *Goldman v. Tesoro Drillling Corp.*, 700 F.2d 249, 251 (5th Cir. 1983); *Alvestad v. Monsanto Co.*, 671 F.2d 908, 912 (5th Cir.), *cert. denied*, 459 U.S. 1070 (1982) and *Union Mechling Corp. v. Carmadelle*, 624 F.2d 677, 679 (5th Cir. 1980). The exception to this rule respecting judgments void *ab initio* does not apply where, as here, only 28 U.S.C. § 455(a) has any relevance to the allegations. *Compare Recreational Properties, Inc. v. Southwest Mortgage Service Corp.*, 804 F.2d 311, 313 (5th Cir. 1986).

[17] No personal rights arise under § 455(a); *cf. Health Services*, 796 F.2d at 800; *Chitimacha Tribe v. Harry L. Laws Co.*, 690 F.2d 1157, 1165 (5th Cir. 1982), *cert. denied*, 464 U.S. 814 (1983); *Kinnear-Weed Corporation v. Humble Oil and Refining Company*, 403 F.2d 437, 439-40 (5th Cir. 1968), *cert. denied*, 404 U.S. 941 (1971). *But see Murphy*, 768 F.2d at 1539-40.

satisfied by requiring a judge who discovers that he has any interest in any creditor to recuse himself prospectively. It would be impractical and inequitable to adopt the remedy suggested by Petitioners that all orders and judgments should be null and void simply because appearances of partiality are alleged. The public interest at stake in bankruptcy cases of prompt, responsible and timely reorganization for the benefit of creditors cannot be ignored. *See In re Timbers of Inwood Forest Associated, Ltd.*, 808 F.2d 363, 373-74 (5th Cir. 1987) (Clark, F. J., concurring), *cert. granted*, 107 S. Ct. 2459 (1987) ("Reorganization is not a Holy Grail to be pursued at any length. Creditors are entitled to a prompt determination of efficacy").

Under the facts of this case, in determining whether a retrospective remedy should be applied, concern about real injustice to the successful litigant, forced to delay or even surrender his decree or judgment and begin again, should on balance outweigh concern about Petitioners' speculation as to an appearance of impartiality. To hold otherwise in this case would result in a windfall in favor of parties who are not even "aggrieved" by the judgment. *See infra.* The rule promoted by Petitioners will do nothing more than encourage losing parties in litigation, even those with "frivolous" claims, to regard § 455 as another strategy for attacking judgments, increase the number of challenges to federal judges and make judgments subject to reconsideration by invoking what a hypothetical unreasonable man might think. *See Delesdernier*, 666 F.2d at 121; *cf. Advisory Opinion* No. 69, *supra.*

POINT II

PETITIONERS HAVE NO STANDING TO APPEAL

The District Court dismissed the appeals of the Committees' Plan because the appellants (including Petitioners herein) lacked standing. The requirements of standing goes to the subject matter jurisdiction of the Court to hear Petitioners' appeal. *See Bender v. Williamsport Area School District*, 475 U.S. 534, 541-49 (1986); *Valley Forge Christian College v. Americans United for Separation of Church & State*, 454 U.S. 464, 488 (1982). The Fifth Circuit affirmed the confirmation orders on the merits without ruling on the issue of standing.

Under existing bankruptcy case law, Petitioners have standing to challenge only those parts of the reorganization plan that affect their direct interest. *See e.g., In re Johns-Manville Corporation*, 68 B.R. 618, 623 (Bankr. S.D.N.Y. 1986); *In re Evans Products Co.*, 65 B.R. 870, 874 (S.D. Fla. 1986); *In re Sweetwater*, 57 B.R. 743, 746 (D. Utah 1985). To have standing to appeal, Petitioners must be aggrieved persons, directly, adversely, and pecuniarily affected by the orders of the Bankruptcy Court. *See, e.g., Sweetwater*, 57 B.R. at 746; *Holywell Corporation v. Bank of New York*, 59 B.R. 340, 349-50 (S.D. Fla. 1986).

The District Court correctly determined that Petitioners were not aggrieved persons. Prior to the Committees' Plan, KHC and KIII were insolvent. This insolvency, admitted repeatedly during the confirmation hearings, was an insurmountable threshold that denied standing to the former shareholders to assert any other issue on appeal. *See In re Evans Products Co.*, 65 B.R. at 874. The District Court thus appropriately ruled that the former shareholders were not aggrieved persons and were without standing to appeal the confirmation of the Committees' Plan.

K. W. Davis, Jr., Kay Davis and Twalla Dupriest, as bankruptcy trustee for the estate of T. C. Davis, hold Class 6 claims. They each had notice of and an opportunity to object to the Committees' Plan and appear in opposition to its confirmation. But, because not a single member of the Davis family filed such an objection to the Committees' Plan or appeared at the confirmation hearing in opposition to the Committees' Plan, the District Court correctly held that these persons failed to preserve their right to appeal. Accordingly, none of the Davis family has a right to be heard for the first time on appeal. *Id.* Moreover, the Class 6 claims have now been paid in full. Petitioners thus are not aggrieved at all in their capacity as Class 6 creditors. For these same reasons, the Petitioners lack standing to seek a retrospective remedy under 28 U.S.C. § 455. They can no more seek a retrospective remedy than could a total stranger to the case.

POINT III

THE COMMITTEES' PLAN HAS BEEN SUBSTANTIALLY CONSUMMATED THEREBY RENDERING PETITIONER'S APPEAL MOOT

On April 16, 1987, in accordance with the self executing provisions of the Committees' Plan, the prior capital stock of KHC was cancelled, KIII was statutorily merged into KHC, a new board of directors and chief executive officer were installed, and new capital stock was issued to the Class 7 creditors. New boards of directors were subsequently elected for all of the KHC subsidiaries. Thereafter, all of the creditors in Classes 1 through 6 under the Committees' Plan were either paid in full or had their rights reinstated, thereby representing full satisfaction of those claims. Further, KHC distributed approximately $40 million in available cash to the Class 7 creditors and made their interest payment aggregating approximately $4.7 million in respect to the notes issued to Class 7

creditors under the Committees' Plan. At no point during the course of the appeal of the confirmation order did Petitioners seek a stay of implementation of the Committees' Plan except for Petitioners' unsuccessful efforts to abate the payment in full of all Class 6 claims.

Federal courts may not resolve questions posited in a vacuum but only those arising in a "case or controversy." *Aetna Life Ins. Co. v. Haworth*, 300 U.S. 227, 239 (1937). In that case the Court stated:

> A "controversy" in this sense must be one that is appropriate for judicial determination. A justiciable controversy is thus distinguished from a difference or dispute of a hypothetical or abstract character; from one that is academic or moot.

Id. at 240. Claims of mootness are controlled by the principles enunciated in *Mills v. Green*, 159 U.S. 651, 653 (1895):

> [W]hen, pending an appeal from the judgment of a lower court, and without any fault of the defendant, an event occurs which renders it impossible for this court, if it should decide the case in favor of the plaintiff, to grant him any effectual relief whatever, the court will not proceed to a formal judgment, but will dismiss the appeal.

The mootness doctrine has been uniformly recognized by the circuit courts in the context of bankruptcy appeals from orders of confirmation. In that context, the "doctrine promotes an important policy of bankruptcy law — that court-approved reorganizations be able to go forward in reliance on such approval unless a stay has been obtained." *See In re Information Dialogues, Inc.*, 662 F.2d 475, 477 (8th Cir. 1981). Thus, when a plan of reorganization has been so substantially consummated that effective relief is no longer available, an appeal is moot and should be dismissed, leaving the order of confirmation and the plan of reorganization as the operative

instruments determining rights among creditors, as well as ownership and management of the company. *See, e.g., id.; Miami Center Ltd. Partnership v. Bank of New York*, 820 F.2d 376, 379 (11th Cir. 1987), *modified on other grounds*, 826 F. 2d 1010 (1987); *In re AOV Industries, Inc.*, 792 F.2d 1140, 1147 (D.C. Cir. 1986); *In re Sun Country Development, Inc.*, 764 F.2d 406, 407 n.1 (5th Cir. 1985); *In re Roberts Farms, Inc.*, 652 F.2d 793, 797 (9th Cir. 1981); *In re Combined Metals Reduction Co.*, 557 F.2d 179, 187, 194 (9th Cir. 1977).

The above facts demonstrate and Petitioners admit in pleadings filed in related proceedings below, that the Committees' Plan has been substantially consummated.[18] Ownership of the corporations has been transferred from the Petitioners, who are the former shareholders, to the creditors. All creditors, with allowed claims, other than Class 7, have been paid in full. Reservations of cash have been made for creditors with contested claims so that if and when those claims are allowed, they will also be paid in full. As the Fifth Circuit aptly stated: "Former stockholders in an insolvent debtor corporation and former management of that corporation, claiming rights or representation of creditors that can now be fully paid, want to vacate a plan of reorganization that has been substantially implemented." Pet. App.-6, 7. Even if this Court were to grant Petitioners' writ of certiorari and decide the case in favor of Petitioners, it would therefore be virtually impossible at this juncture to grant any effective relief. As a result, this appeal is moot and does not present a justiciable controversy.

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[18] *See* Brief of Appellants, *In re: Kendavis Holding Co., et al.*, CA No. 3-87-2561-G (U.S.D.C., N.D. Texas) filed Nov. 17, 1987 and Emergency Application for Writ Pursuant to 28 U.S.C. § 1651(a) and Supporting Brief, *In re: Kendavis Holding Co., et al.*, No. 87-1687 (5th Cir.) filed September 11, 1987.

CONCLUSION

For the above and foregoing reasons, it is respectfully submitted that this Honorable Court should deny the Petition for Writ of Certiorari.

Respectfully submitted,

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CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

IN RE KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC.,

Debtors

K. W. DAVIS, JR., ALANA LAWLER, ALANA LAWLER TRUST "A", A. T. DAVIS, A. T. DAVIS TRUST "A", KAY DAVIS, KAY DAVIS TRUST "A", TRICIA KAE LAWLER, ALANA LAWLER CHILDREN'S TRUST, ALLEN KENNETH DAVIS, JANIECE BREANNE DAVIS, A. T. DAVIS CHILDREN'S TRUST, KAY DAVIS CHILDREN'S TRUST, T. C. DAVIS, II, T. C. DAVIS, II TRUST, T. C. DAVIS, II TRUST "A", T. C. DAVIS, II TRUST "A" DATED JANUARY 15, 1982, BRIAN KEITH DAVIS, BRIAN KEITH DAVIS TRUST, BRIAN KEITH DAVIS TRUST "A", BRIAN KEITH DAVIS TRUST DATED JANUARY 15, 1982, CHESLEY DAVIS, CHESLEY DAVIS TRUST, TREY DAVIS, TREY DAVIS TRUST, KEN W. DAVIS FOUNDATION AND TWALLA DUPRIEST, TRUSTEE FOR ESTATE OF T. C. DAVIS,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY, KENDAVIS INDUSTRIES INTERNATIONAL, INC. AND LOFFLAND BROTHERS COMPANY, KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, THE BANK OF NOVA SCOTIA AND MBANK HOUSTON, N.A.,

Respondents

RESPONDENT OFFICIAL UNSECURED CREDITORS' COMMITTEES SUPPLEMENTAL BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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No. 87-846

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1987

K. W. DAVIS, JR., ET AL.,

Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES, ET AL.,

Respondents

RESPONDENT OFFICIAL UNSECURED CREDITORS' COMMITTEE'S SUPPLEMENTAL BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondent Official Unsecured Creditors' Committees of Kendavis Holding Company, Kendavis Industries International, Inc. and Loffland Brothers Company (the "Respondent Committees") respectfully submit the following Supplemental Brief pursuant to Rule 22.6 of the Rules of the Supreme Court for the United States.

Shortly after filing the Respondent Unsecured Creditors' Committees' Brief In Opposition to Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit, the undersigned discovered that an order and memorandum of decision were entered by a trial judge which may affect the status of *NEC Corp. v. Intel Corp.*, 654 F. Supp. 1256 (N.D. Cal. 1987), *mand. docketed,* No. 87-7126 (9th Cir. Mar. 30, 1987),[1] cited in the following, to wit: (i) Respondent Committees' Brief in Opposition to Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit at 9 and 10; (ii) Respondent Kendavis Holding Company's Brief in Opposition to Petition for Writ of Certiorari at 9, 18 and 19;

[1] The order of recusal may render the mandamus action to the Ninth Circuit moot.

and (iii) Petitioners' Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit at 17 n.26. *See* R.Supp.App.-1a for a copy of the court's memorandum of decision.

Neither the memorandum of decision nor the order of recusal state the statutory grounds for the court's recusal. *See* R.Supp.App.-1a and 2a. Therefore, because Respondent Committees are not aware of any of the factual circumstances surrounding the court's recusal in *NEC v. Intel,* Respondent Committees are not in a position at this time to comment further.

Respectfully submitted,

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APPENDIX

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

NEC CORPORATION, a Japanese corporation, and NEC ELECTRONICS INC., a California corporation,

Plaintiffs,

v.

INTEL CORPORATION, a California corporation,

Defendant.

No. C-84-20799-WAI

ORDER OF RECUSAL

I, the undersigned Judge of this court, finding myself disqualified in the above-entitled matter within the meaning of (F)(2) of the Assignment Plan of this court, request that this case be reassigned.

All orders previously made and entered in the above-entitled action are vacated and set aside.

Dated: December 15, 1987

/s/ WILLIAM A. INGRAM

William A. Ingram
United States District Judge

Supreme Court, U.S.
FILED
JAN 9 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-846

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

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Petitioners

v.

THE OFFICIAL UNSECURED CREDITORS' COMMITTEES FOR KENDAVIS HOLDING COMPANY AND KENDAVIS INDUSTRIES INTERNATIONAL, INC., KENDAVIS HOLDING COMPANY, FEDERAL DEPOSIT INSURANCE CORPORATION, BANK OF NOVA SCOTIA, AND MBANK HOUSTON, N.A.

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REPLY BRIEF OF PETITIONERS

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

NO. 87-846

K. W. DAVIS, JR., ET AL.,

Petitioners

v.

OFFICIAL UNSECURED CREDITORS' COMMITTEES ET AL.,

Respondents

REPLY BRIEF OF PETITIONERS

Petitioners submit this brief in reply to the briefs filed by the Official Unsecured Creditors' Committees of Kendavis Holding Company and Kendavis Industries International, Inc. ("Committees"), Kendavis Holding Company ("KHC"), and The Bank of Nova Scotia ("Scotia").[1]

ARGUMENT IN REPLY

1. The Bankruptcy Judge Was Disqualified Under 28 U.S.C. § 455(a) and (b)(4) and the Order of Confirmation Should Be Vacated.

Respondents seriously misrepresent Petitioners' argument on a vital point. Petitioners do not charge a judge with a duty

[1] Of the other interested parties only the First Interstate Bank of California has responded by adopting the Committees' response.

to *insure* that he or she does not participate in any case in which he or she owns a financial interest in a party. Petitioners do argue that "the combination of § 455(b)(4)(1982) and the duty to be informed as to personal and fiduciary investments under § 455(c) establish a standard by which a judge is charged, conclusively, with knowledge of that which information in his possession reveals about his financial interest or which reasonable inquiry would reveal." Petition p. 15. Petitioners agree that the decisions in *Hodosh v. Block Drug Co., Inc.*, 790 F.2d 880 (Fed. Cir.), *cert denied*,____ U.S. ____, 107 S.Ct. 106 (1986) and *Union Carbide Corp. v. U.S. Cutting Serv., Inc.*, 782 F.2d 710 (7th Cir. 1986) were not vulnerable to attack on disqualification grounds. In neither case did the judge possess information disclosing that the judge's spouse owned stock in a party (in *Hodosh*, the judge's wife owned stock in a corporation which acquired an appellant pending appeal and, in *Union Carbide*, the judge's husband owned stock in two unnamed members of a 172,000 putative, uncertified class). *In re Indus. Gas Antitrust Litig.*, No. 80-C-3479 (N.D.Ill.E.D. Sept. 24, 1985), (Westlaw p. 2). There was no suggestion of oversight, neglect, or forgetfulness. In both cases the judge's duty was only to make reasonable inquiry as to the spouse's financial interest. Here the duty under § 455(c) is that the judge "should inform himself" of his own financial interests and Judge McGuire regularly received information revealing the ownership of Morgan Guaranty Trust Co. ("Morgan Guaranty") by J.P. Morgan Co., Inc. ("J.P. Morgan"). See Petitioners' Appendix pp. 19 and 25 ("Pet. App." hereafter).

Respondents also argue that Petitioners (and, inferentially, all Respondents, and other creditors including Morgan Guaranty) could have discovered Judge McGuire's financial interest by perusing his publicly-filed Financial Disclosure Reports and, thus, the objection comes too late. In *United*

States v. State of Alabama, 828 F.2d 1532 (11th Cir. 1987), the court addressed the timeliness question in an extensive footnote. 828 F.2d 1544, n. 49. The court noted some split of authority but stated "appellants did not discover relevant information about Judge Clemon's activities as a state legislator until late in the litigation, and raised this ground for disqualification at the first available moment." Similarly, in this case, after learning of the grounds for disqualification on March 23, 1987, Petitioners moved for relief on March 31, 1987. In no way did Petitioners delay after acquiring the disqualifying information. Although in *United States v. State of Alabama* the issue was raised before trial, the difficulty, complexity, and burdens on the parties of reversal would be identical with this case where it was promptly raised after acquiring knowledge (knowledge previously available to the trial judge).[2]

---

[2] No party in these proceedings has alleged that Petitioners or any of their representatives at any time prior to March 23, 1987, knew that the judge owned stock in J.P. Morgan. Indeed, records kept by the bankruptcy clerk's office and acquired by other counsel for Petitioners, revealed that no party to this litigation had made inquiry prior to Judge McGuire's announcement on March 23, 1987, and that only one or two news gathering services had viewed such reports previously. This information is not of record but reveals some of the difficulties in denying Petitioners any relief without a due process hearing. Petitioners, in their *amici curiae* brief in *Liljeberg v. Health Servs. Acquisition Corp.* (Supreme Court docket No. 86-957), acknowledged that estoppel might be applicable to a party who had unreasonably delayed seeking the disqualification of a judge after the knowledge had been acquired. In this case, however, it is clear that Petitioners acted promptly in not only raising the issue but in attempting to discover all of the pertinent facts. In any event, the duty to recuse under 28 U.S.C. § 455 is that of the judge who in fact had all the pertinent information.

Respondents also suggest that compliance with 28 U.S.C. § 455(b)(4) by a bankruptcy judge may be extremely difficult in cases where there are tens of thousands of creditors. But the argument is inapposite. Here we are dealing with a signatory to the involuntary petition and a major and active creditor, which is one of 11 members of the KHC committee, one of 26 Class 7 creditors, and one of approximately 78 total creditors of KHC and KIII. See Respondents' Joint Appendix. pp. 15-17. ("Resp. Jt. App." hereafter).

2. The Petitioners Have Standing To Challenge Orders Entered By A Judge Disqualified Pursuant To 28 U.S.C. § 455 Which Order Cancelled Their Corporate Securities and Removed Them From Control of The Corporation.

Respondents contend Petitioners lack standing to challenge the orders confirming the plan of reorganization. Standing is absent, so Respondents say, because Petitioners are not aggrieved. They are not aggrieved, it is contended, because KHC is insolvent, the insolvency finding is not challenged, and, consequently, Petitioners do not stand to benefit from appellate review.[3] Below Respondents argue

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[3] Respondents allude to the failure of Petitioners to appear or object to proceedings in the bankruptcy court. The Petitioners at all times in the bankruptcy court proceedings were closely identified with the debtors KHC and KIII. The Petitioners were all of the shareholders of KHC, including the directors of KHC, and three of the Petitioners were the principal officers of KHC. Ken W. Davis, Jr., as president and chief executive officer and Kay Davis as corporate secretary of KHC, were present throughout the confirmation hearings and consistently worked with debtors' counsel in formulating the objections to the confirmation of the plan presented to the bankruptcy court. Where the identical objection and argument raised on appeal have been made by a similarly aligned party, the requirement of a second, "me too" objection serves no purpose. *Hormel v. Helvering*, 312

that under the "absolute priority rule" derived from *Case v. Los Angeles Lumber Prods. Co.*, 308 U.S. 106 (1939), and as modified by Bankruptcy Code § 1129(b), 11 U.S.C. § 1129(b) ("Code" hereafter), shareholders of an insolvent debtor corporation are not entitled to receive anything. But this is overly simplistic. *If and when* appropriate findings of certain predicate facts are entered by a judge not disqualified by interest, such shareholders *may* receive nothing in bankruptcy. But the predicate facts to such a result involve, *inter alia*, compliance with Code § 1129(a), requiring a host of judicial findings. 5 *Collier on Bankruptcy* ¶ 1129.03[e] (15th Ed. 1987) and G. Triester, J. Trost, L. Forman, K. Klee & R. Levin, *Fundamentals of Bankruptcy Law*, § 9.04(d)(2) (1986). Petitioners have contended that the plan confirmed did not meet Code § 1129(a) and that the judge making the requisite findings and entering the order of confirmation owned a disqualifying interest. If Petitioners' equity is to be cancelled,[4] they are entitled to have it done according to law and by a disinterested judge.

U.S. 552, 556-59; and *In re Brio Petroleum, Inc.*, 800 F.2d 469 (5th Cir. 1986). In any event, Petitioners separately raised the issue of judicial disqualification.

[4] Petitioners' rights to control the corporation, to seek to reorganize, to sell the stock (see e.g. *Jones v. McSpedden*, 560 S.W.2d 177 (Tex. Civ. App. 1977) (stock in an insolvent corporation is a sufficient consideration to support a contract)), to sell the assets (see e.g. *Calnan v. Guaranty Sec. Corp.*, 171 N.E. 830 (Mass. 1930) (shareholders of an insolvent corporation may sell the assets)) and to seek future business opportunities were also terminated by the bankruptcy court orders challenged herein. Bankruptcy courts have recognized that equity securities in a corporation with a negative balance sheet value are property of the estate and are not valueless. (*In re Landau Boat Co.*, 8 B.R. 436 (Bankr. W.D. Mo. 1981) and *In re Modern Glass Specialists, Inc.*, 42 B.R. 139 (Bankr. E.D. Wis. 1984)).

Moreover, standing to participate on any issue is granted by Code § 1109. The Petitioners herein are bound by the challenged orders. Code § 1141. If Petitioners are to be bound by the bankruptcy court orders, they are entitled to challenge those orders on appeal. *West v. Radio-Keith-Orpheum Corp.*, 70 F.2d 621, 623 (2nd Cir. 1934).

To deny Petitioners standing also results in a major shift of emphasis in chapter 11 corporate cases. "Usually bankrupts are insolvent . . . ." Jordan and Warren, *Bankruptcy* 2 (1985). If so, early in a case, senior creditors, by moving for a valuation of the estate, could override Code § 1109 and exclude equity security holders from participation. Rather than be encouraged to use chapter 11 to restructure debt, debtor corporations, under control of equity owners, would be reluctant to expose themselves to the possibility that filing would result in their exclusion from the reorganization process.

It is abundantly clear that both the "case or controversy" requirements of standing derived from article III of the United States Constitution,[5] and the prudential principles derived from concepts of judicial efficiency,[6] are satisfied here.

3. The Issues Presented In This Petition Are Not Moot.

Respondents argue that the issues presented herein have become moot while Petitioners' appeals were pending. If performance of a plan of reorganization renders appeals of the order of confirmation moot, then dissenting interest holders are effectively deprived of appellate review in the

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[5] *Simon v. Eastern Kentucky Welfare Rights Org.*, 426 U.S. 26 (1976).

[6] *Valley Forge Christian College v. Americans United for Separation of Church and State, Inc.*, 454 U.S. 464 (1982).

absence of a stay. In complex cases, such as this one, the discretionary denial of a stay, or onerous bonding requirements (a minimum of $300 million was requested by Respondent Committee in the Fifth Circuit) will result in appeals on grounds involving Code § 1129(a) usually becoming moot before appellate review can occur. Note, *Mootness on Appeal in the Supreme Court,* 83 Harv. L. Rev. 1672, 1692 (1970).

The Fifth Circuit did not rely on mootness. See Pet. App.-6. The alleged mootness is based on factors described in the Amended Affidavit of David E. Hawthorne. Resp. Jt. App.-12. These events were steps taken to implement the plan, or in some instances steps taken to accelerate the terms of the plan, and steps taken at the corporate subsidiary level independent of any plan provision. In summary, these steps are as follows: 43 holders of undisputed claims in Classes 1-5 have been paid about $1.5 million (or retain their claims unaffected by the plan). Nine holders of undisputed claims in Classes 6 were paid their first one-third installment of about $294,000. Resp. Jt. App. 16-17. Based on a motion to accelerate payment of the remaining installments to Class 6 creditors, the remaining Class 6 undisputed claims have been paid.[7] Remaining, disputed claims are being resolved.

The Committees' members and other institutional creditors fall in Class 7. These 26 creditors have received new KHC common and preferred stock, new KHC long- and short-term notes, and about $44.4 million in cash. Resp. Jt. App.-15-16. Additionally, KIII has been merged into KHC, new directors and officers have been selected for KHC, new directors have been selected for all KHC subsidiaries, and

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[7] The Petitioners have appealed to the district court the bankruptcy court order allowing this accelerated payment of $494,000. *In re Kendavis Indus. Int'l, Inc., et al.*, appeal docketed, No. CA3-87-2561-G (N.D. Tex. Dallas Div. 1987).

new officers have been selected for many KHC subsidiaries. Resp. Jt. App.-14, 18-20. Pending involuntary bankruptcy petitions against 12 KHC subsidiaries have been dismissed without prejudice. Other steps are described in the Amended Hawthorne Affidavit.

Petitioners agree that appeals are moot in bankruptcy cases where sufficient steps have been taken such that the appellate court could not give effective relief if reversal were in order.[8] But Respondents also argue that where a stay is not granted, a bankruptcy appeal case is mooted by substantial consummation. None of their cases support this proposition.

The rule of the cited cases and others is that an appeal becomes moot when new value is invested in the reorganized debtor by third parties who rely in good faith on the order appealed, where third parties necessary for appellate relief are not before the court, or where assets have been sold and no stay obtained. Indeed, Petitioners believe the sole test for mootness in such cases is whether the parties necessary for effective relief are before the court.[9] Nothing here calls for new value to be invested or the sale of assets pursuant to the plan. All parties necessary for effective relief are before the Court. Federal courts have adequate authority to retrieve consideration,[10] undo mergers,[11] or grant other appropriate

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[8] *Mills v. Green*, 159 U.S. 651 (1895).

[9] Where assets are sold and no stay obtained, the sale to a good faith purchaser may not be reversed. Code § 363(m). Thus the court cannot give effective relief when the sale is challenged and such an appeal becomes moot.

[10] *County of Dakota v. Glidden*, 113 U.S. 222 (1885).

[11] *Standard Oil Co. of New Jersey v. United States*, 221 U.S. 1 (1911); *United States v. Brown Shoe Co.*, 179 F.Supp. 721 (E.D. Mo. 1959), *aff'd* 370 U.S. 294 (1962); *Ramsburg v. American Inv. Co.*, 231 F.2d

relief where they have jurisdiction over the proper parties. Where some but not all matters are beyond effective appellate relief, the matters within the court's appellate control are not moot.[12] Here, all Class 7 creditors who have received or are to receive all the new common and preferred stock, long- and short-term notes totaling approximately $65.5 million, and all Available Cash, and whose aggregate claims of in excess of $500 million dwarf the remaining claims (see Committees' Brief p. 8, n. 3), are parties to the appellate process. There is no difficulty in this Court requiring the return of any consideration received by these parties or undoing the merger of KHC and KIII.

In any event, the "established practice of the Court in dealing with a civil case from a court in the federal system which has become moot while on its way here or pending our decision on the merits is to reverse or vacate the judgment below and remand with direction to dismiss." *United States v. Munsingwear*, 340 U.S. 36, 39 (1950). This is necessary "to prevent a judgment, unreviewable because of mootness, from spawning any legal consequences." *United States v. Munsingwear*, 340 U.S. at 41. Thus, if the Court believes the issues herein have become moot, Petitioners request this Court to grant the writ of certiorari, vacate the judgment, and remand the case to the court of appeals with instructions that the bankruptcy court dismiss the case as moot. *Delta Airlines, Inc. v. International Brotherhood of Teamsters, et al.*, ____ U.S. ____, 108 S.Ct. 53 (1987) and *Russoniello v Olheues*, _____ U.S. ____, 108 S.Ct. 52 (1987).

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333 (7th Cir. 1956); and *Fink v. Continental Foundry and Machine Co.*, 240 F.2d 369 (7th Cir. 1957).

[12] In re *AOV Indus., Inc.*, 792 F.2d 1140 (D.C. Cir. 1986) and *In re King Resources*, 651 F.2d 1326 (10th Cir. 1980).

CONCLUSION

Petitioners request this Court to grant a writ of certiorari and review the instant decision of the United States Court of Appeals for the Fifth Circuit on the merits or, alternatively and if this Court concludes the issues herein are moot, to grant the writ, vacate the orders below and remand to the Fifth Circuit with instructions to direct the bankruptcy court to dismiss the case.

Respectfully submitted,

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